Supreme Court, U.S.
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IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1997

COLEMAN OIL COMPANY, INC., a New Hampshire corporation,

Petitioner,

v.

THE CIRCLE K CORPORATION, et al.,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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103 pp

QUESTION PRESENTED FOR REVIEW

Whether a bankruptcy court has the implied, non-statutory authority to abrogate fundamental contract rights by altering the terms of an existing contract on the grounds that such alterations "effectuate the objectives of 11 U.S.C. §365" by allowing a debtor to renew an executory contract when its prior defaults would otherwise prevent it from doing so?

LIST OF PARTIES

The parties are the petitioner, Coleman Oil Company, Inc., a New Hampshire corporation ("Coleman") and Respondents, The Circle K Corporation, Circle K Convenience Stores, Inc., Circle K Management Company, Lar-lin, Inc., First Circle Properties, Inc., Utotem, Inc., Utotem Markets of Arizona, Inc., U Totem of Alabama Inc., U-tote'm of Colorado Inc.,U-tote-m of Miami, Inc., Tic Toc Systems, Inc., Monterre Properties, Inc., Shop & Go, Inc., Circle K General, Inc., Circle K Hawaii, Inc., Combined Aviation Co., Charter Marketing Company, Charter Marketing Company (Connecticut), Mr. B's Oil Co., Inc., Mr. B's Food Mart, Inc., NPI Corporation, Old Colony Petroleum Company, Inc., New England Petroleum Distributors, Inc., and 44th Street & Camelback Limited Partnership ("Debtors").

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PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
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PETITION FOR WRIT OF CERTIORARI

The Petitioner, Coleman Oil Company, Inc. respectfully requests that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit, filed October 22, 1997.

DISCUSSIONS AND OPINIONS OF LOWER COURTS

On April 6, 1994 the United States Bankruptcy Court for the District of Arizona issued its Order granting summary judgment in favor of Debtors New England Petroleum Distributors, Inc. and Old Colony Petroleum permitting the assumption of certain leases of real property owned by Coleman. Coleman Oil Company, Inc., a New Hampshire Corporation, Plaintiff v. The Circle K Corporation, et al., Defendants ("In re Circle K Corporation, et al."), Chapter 11, Case Nos. B-90-5052 PHX GBN to B-90-5075 PHX GBN (Jointly Administered), Adversary No. 91-974-GBN, docket at 73 (Bankr. D. Ariz., April 6, 1994). The Order was not officially reported but has been reprinted in the Appendix at

page 1a.

Coleman appealed the Order to the Bankruptcy Appellate Panel for the Ninth Circuit ("BAP") which affirmed the lower court in a split decision with opinions written by both the majority and dissenting judges. An initial decision was released by the BAP on December 11, 1995, but an amended Opinion was issued on January 8, 1996. The BAP Opinion is reported at 190 B.R. 370 (Bankr. 9th Cir. 1996), and is reprinted in the Appendix at page 9a.

The matter was appealed to the Ninth Circuit Court of Appeals which affirmed the BAP, again in a split decision. The Ninth Circuit Opinion, filed on October 22, 1997, is reported at 127 F.3d 904 (9th Cir. 1997) and is reprinted in the Appendix at page 43a.

JURISDICTION

The United States Court of Appeals for the Ninth Circuit filed its Opinion on October 22, 1997. The jurisdiction of this Court to review the decision of the United States Court of Appeals for the Ninth Circuit is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

This Petition involves the proper interpretation of 11 U.S.C. §365 which has been reproduced in its entirety in the Appendix at page 60a.

STATEMENT OF THE CASE

In 1977, Coleman Oil Company ("Coleman") leased to Pickering Oil Heat, Inc. ("Pickering") six retail gasoline stores located in New Hampshire and Maine. Through a series of acquisitions and mergers, two subsidiaries of the Circle K Corporation eventually claimed to be the holders of the leasehold interests originally held by Pickering. Each identical lease agreement provided for a ten year term with options to renew for two additional five year terms, provided that none of the leases were in default at the time the options

were exercised.

On May 15, 1990, the Circle K Corporation and its subsidiaries ("Debtors") filed a Chapter 11 bankruptcy petition and immediately requested an extension of the 60-day deadline in which to assume or reject the Coleman leases pursuant to 11 U.S.C. §365(d)(4). The Bankruptcy Court granted the extension which ultimately continued for nearly three years.

In 1992 the Debtors attempted to exercise the second renewal option to extend the terms of the Coleman leases, even though defaults in at least some of the leases existed. In March and April of 1993, the Debtors filed motions to assume the Coleman leases and subsequently filed a motion for summary judgment with respect to the issues raised in the assumption motions. Federal jurisdiction over the dispute was invoked pursuant to 11 U.S.C. §157(b). The Bankruptcy Court granted the Debtors' motion for summary judgment by Order dated April 6, 1994 ("Order") and permitted the Debtors to assume the leases.

Coleman appealed the Order to the Bankruptcy Appellate Panel for the Ninth Circuit ("BAP"). The BAP affirmed, holding that Coleman had failed to raise a material issue of fact regarding the Debtors' status as assignees of the leases and that the Debtors' exercise of the two renewal options was valid even though defaults existed at the time of the second extension. Judge Barry Russell dissented, concluding that Section 365 of the Bankruptcy Code did not authorize the Bankruptcy Court to modify the express terms of the leases.

Coleman appealed to the Ninth Circuit Court of Appeals which affirmed the BAP's decision. The Ninth Circuit held that the Debtors could exercise their final option to renew the leases without first curing their pre-petition defaults, stating that "no principle of bankruptcy or contract law precludes us from permitting the Debtors here to extend their leases in a manner contrary to the leases' terms, when to do so will effectuate the purposes of section 365." 127 F.3d at 911. Judge Pamela Ann Rymer dissented in part, opining that

nothing in 11 U.S.C. §365 allows debtors to disregard the requirements of their leases and renew while in default.

REASONS FOR GRANTING THE WRIT

I. THIS CASE PRESENTS AN IMPORTANT QUESTION OF FIRST IMPRESSION REGARDING THE EXTENT TO WHICH THE BANKRUPTCY COURT HAS THE IMPLIED AUTHORITY TO ABROGATE EXISTING CONTRACT RIGHTS.

Private contract rights should not be lightly regarded by the courts. As this Court has recognized, "[m]arket efficiency requires effective means to enforce private agreements." American Airlines, Inc. v. Wolens, 513 U.S. 219, 230, 115 S.Ct. 817, 824 (1995). Consequently, courts should be extremely reluctant to alter private contract rights on the basis of a perceived need to "effectuate" a statute which does not expressly provide for such a result.

Without question, there are provisions within the Bankruptcy Code which can have an impact on private contract rights. For example, 11 U.S.C. §362 imposes an automatic stay upon the filing of a bankruptcy petition which prevents creditors from taking any action to enforce their contract rights against the debtor without first obtaining relief from the Bankruptcy Court. 11 U.S.C. §365(e) generally prevents the enforcement of provisions which make the filing of a bankruptcy grounds for terminating or modifying an executory contract or unexpired lease. Ultimately, 11 U.S.C. §727 allows bankruptcy debtors to completely discharge pre-petition contract obligations. All of these provisions have one thing in common — each represents a circumstance where Congress has made an express determination that the benefits to be gained from a national bankruptcy policy outweigh the preservation of private contract rights.

The implication by a bankruptcy court of the power to alter existing contracts in furtherance of a debtor's efforts to reorganize creates two significant problems. First, it injects bankruptcy courts into the legislative arena, requiring the

court to assume that the absence of express statutory language was accidental and forcing it to anticipate how Congress would have weighed the interest in enforcing private contracts against a bankruptcy policy favoring the reorganization of debtors. Second, it adversely impacts private market forces by adding unpredictability to the contract formation process. When Congress enacts a law that affects private contract rights, a sophisticated marketplace will account for this impact and place a monetary value on it. However, when a court finds the implied authority to modify contract rights, the results are far less predictable and the market is less able to make an appropriate adjustment.

In the present case, the Ninth Circuit has held as a matter of first impression that a bankruptcy debtor is not bound by an unambiguous provision in an executory lease which requires it to cure all defaults as a condition for exercising a renewal option. Prior to this case, no court had ever addressed this specific legal issue. As Judge Rymer noted in her dissenting opinion below, "[t]he path to deciding whether 11 U.S.C. §365 allows a lessee debtor in bankruptcy to exercise an option to renew despite being in default, contrary to an express condition precedent in the lease, is uncharted." 127 F.3d at 911. It is respectfully submitted that by answering this question in the affirmative, the panel majority has made a wrong turn.

II. THE NINTH CIRCUIT COURT OF APPEALS DECISION DEPARTS FROM ALL RECOGNIZED RULES OF STATUTORY CONSTRUCTION

11 U.S.C. §365 permits the assumption or rejection of an executory contract or lease. It does not empower a court to rewrite contractual terms. In this case, the Ninth Circuit has sanctioned the abrogation of contractual rights and has sweepingly held that bankruptcy policy justifies such interference. Nowhere has Congress expressly granted such authority to the Bankruptcy Court.

The leases at issue provide as follows:

> Lessee shall have two (2) additional and successive terms of five (5) years . . . , by giving Lessor at least six (6) months written notice . . . , provided that Lessee's right to extend is conditioned upon the Lessee not being in default hereunder and is not in default of payments under any of the other leases . . . (emphasis added).

Thus, there were two conditions precedent to exercising the renewal option: notice and an absence of default. Although there is no dispute that the Debtors failed to meet the second prerequisite, the courts below determined that the option could be exercised and the term of the leases extended. In so ruling, they effectively excised a material provision of the parties' agreement and substituted a judge-made term. This is a step which is not contemplated by the Bankruptcy Code and which can only lead to unpredictability in the commercial marketplace.

This petition should be granted because the Ninth Circuit decision violates fundamental principles of statutory construction. It creates out of whole cloth a rule of law which effectively authorizes the bankruptcy court to modify executory contracts whenever doing so would assist a debtor's efforts to reorganize.

A. Section 365 of the Bankruptcy Code Contains No Provision Supporting the Ninth Circuit's Ruling.

The Ninth Circuit majority attempts to characterize its decision as an interpretation of 11 U.S.C. §365. However, as Judge Rymer aptly noted in her dissent,

> . . . nothing in §365 . . . allows debtors to disregard their leases and renew while in

default. . . .

> Section 365 does not extend the time to exercise the option or to meet conditions precedent. Nor does §365 give the debtor the right to opt to renew a contract that is in default when the contract by its terms requires that a default first be cured. To hold otherwise rewrites the lease and, as I read it, §365. 127 F.3d at 911.

Similarly, Judge Russell, dissenting from the BAP decision stated,

> I know of no provision in the Bankruptcy Code which gives a debtor in possession the right to exercise an option without also curing any default as required by the very contract which gives the lessee the right to exercise the option. Although the majority argues that §365 abrogates an important right of the lessor in the lease, i.e., the right to have all defaults cured when the option is exercised, they point to no specific part of §365 to achieve this result.
>
> There is nothing in §365 that extends the time to exercise the option and the fulfillment of any conditions precedent, such as not being in default, at the time of the purported exercise. 190 B.R. at 379.

A review of §365 substantiates the dissenters' position. Nevertheless, the Ninth Circuit majority reasoned that rewriting a contract is permissible because "all kinds of interferences with contractual rights occur in bankruptcy proceedings." 127 F.3d at 910. It cited as support for this proposition §365(a) which permits the rejection of an entire contract, the automatic stay, and the debtor's ability to cure a default even though the contract does not provide for cure. But, in each of these cases, Congress has specifically delineated an exception to the enforcement of a contractual term. For example, the fact that ipso facto clauses are unenforceable is explicitly set forth in §365(e). The debtor's power to assume or reject and to cure defaults is expressly provided for in §365(a) and (b). Obviously, when Congress desired to permit a contractual modification in bankruptcy, it so legislated. Nothing in §365 remotely suggests that Congress has authorized the court to abrogate a nondebtor party's contract rights on an ad hoc basis. In fact, the legislative history of §365 supports just the opposite conclusion:

> The unenforcibility of ipso facto or bankruptcy clauses proposed under this section will require the courts to be sensitive to the rights of the nondebtor party to executory contracts and unexpired leases. If the trustee is to assume a contract or lease, the court will have to insure that the trustee's performance under the contract or lease gives the other contracting party the full benefit of his bargain. H.R. Rep. No. 95-595, 95th Cong., 1st Sess., 348-9 (1977). See Senate Report No. 95-989, 95th Cong., 2d Sess. 59 (1978). (emphasis added)

This Court has recognized that Congress did not intend for

the Bankruptcy Code to obliterate general contract law. Congress has repeatedly expressed its legislative determination "that the trustee [or debtor-in-possession] is not to have carte blanche to ignore non-bankruptcy law." U.S. v. Ron Pair Enterprises, Inc., 489 U.S. 235, 244, citing Midlantic National Bank v. New Jersey Department of Environmental Protection, 474 U.S. 494, 502 (1986).

Other courts addressing similar facts have also recognized their limited authority to modify private contracts. For example, in In Re Cook United, Inc., 53 B.R. 342, 345 (Bankr.N.D.Ohio 1985), the court stated:

> Debtor is requesting this Court to rewrite the leases and Section 365 of the Bankruptcy Code, by holding that even though it was in default, Debtor had a right to exercise its option to renew the leases prior to its assuming said leases and curing the defaults. This Court cannot do so. The bankruptcy court has no authority to modify or nullify contractual provisions ... Matter of Schokbeton Indus., Inc., 466 F.2d 171 (5th Cir. 1972). . . .
>
> To allow Debtor to exercise the option without assuming the lease would be a substantial interference with the contractual rights of the lessor, because he would not know if the lessee intended to remain, the very thing for which he bargained. Where the lessor has requested assumption or rejection, Debtor must assume before it

> may exercise an option to renew. In order for Debtor to reap the benefits of a contract, it must at the same time bear the burdens of that contract. In re Tirenational Corp., 47 B.R. 674 (Bankr.N.D.Ohio 1985). (emphasis added)

Therefore, the Ninth Circuit's interpretation of §365 violates an accepted maxim of statutory construction, expressio unius est exclusio alterius — the expression of one thing is the exclusion of another. U.S. Term Limits, Inc. v. Thornton, 514 U.S. 779, 793 fn. 9 (1995); Lectherman v. Tarrant County Narcotics Intelligence And Coordination Unit, 507 U.S. 163, 168 (1993). Congress has dictated that certain contract modifications are warranted in furtherance of bankruptcy policy. These are set forth in the Bankruptcy Code. Congress did not provide for court-orchestrated contractual bargaining. That is what occurred in this case when the Ninth Circuit advocated a rule of law permitting the Bankruptcy Court to override the parties' agreement in order to "effectuate" §365.

B. The Ninth Circuit's Ruling Is Contrary to Principles Embodied in the Bankruptcy Code.

The Ninth Circuit found "'the purpose behind §365 is to balance the state law contract right of the creditor to receive the benefit of his bargain with the federal law equitable right of the debtor to have an opportunity to reorganize.' ... The lessor will then get the benefit of its bargain upon assumption, when the debtor lessee must cure the defaults." 127 F.3d at 909, quoting from BAP Opinion, 190 B.R. at 376.

But this ruling is a derogation of principles embodied in §365 and other sections of the Bankruptcy Code. The property of a debtor, including contractual rights, enters the bankruptcy estate intact. The Seventh Circuit has stated:

> [W]hatever rights a debtor has

> in property at the commencement of the case continue in bankruptcy — no more, no less. Section 541 is not intended to expand the debtor's rights against others more than they exist at the commencement of the case.

Moody v. Amoco Oil Co., 734 F.2d 1200, 1213 (7th Cir. 1984) citing H.R. Rep. No. 595, 95th Cong., 1st Sess., reprinted in 1978 U.S. Code Cong. & Ad. News 5787. See also In re Thomas, 883 F.2d 991, 995 (11th Cir. 1989), cert. denied, 497 U.S. 1007 (1990).

More specifically, several Circuits including the Ninth , are in accord that nothing in the Bankruptcy Code enlarges a debtor's rights to extend the term of an executory contract.

> The automatic stay does not toll the mere running of time under a contract, and thus it does not prevent automatic termination of the contract ... Section 362 does not give a debtor greater rights in a contract. Thus, debtors cannot rely on Section 362 to prevent termination of the contracts. Moody v. Amoco Oil Co., 734 F.2d at 1213.

See also Hazen First State Bank v. Speight, 888 F.2d 574, 576 (8th Cir. 1989); In re Carroll, 903 F.2d 1266, 1271 (9th Cir. 1990).

Similarly, the First Circuit in In re Gull Air, Inc., 890 F.2d 1255, 1262 (1st Cir. 1989) held that "when a debtor's proprietary interest expires by operation of an express condition, the Bankruptcy Code does not preserve that interest and prevent termination." See also In re Advent Corp., 24 B.R. 612, 614 (Bankr. 1st Cir. 1982) ("The

Bankruptcy Code neither enlarges the rights of a debtor under a contract, nor prevents the termination of a contract by its own terms."); In re G-N Partners, 48 B.R. 462, 466 (Bankr. D. Minn. 1985) ("Nothing in §365 gives the trustee the right to extend indefinitely a time provision in an option any more than a trustee could extend the right to occupancy under a lease past the stated lease period by purporting to assume it."); In re Internet Realty Partnership, 26 B.R. 383 (Bankr.E.D.Pa. 1983) ("Time is always of the essence in an option contract and, unless exercised, an option expires on the specified date ... The filing of a petition for reorganization under Chapter 11 does not expand the rights of the debtor under an option agreement.").

The Ninth Circuit's decision permitting bankruptcy courts to engage in arbitrary contractual redrafting does not square with this well-settled principle that the material terms of a pre-petition contract are to be preserved. It essentially authorizes bankruptcy courts to rewrite executory contracts whenever doing so would enhance a debtor's ability to reorganize.

In addition, the Ninth Circuit's ruling does not comport with another well-established principle that a debtor cannot elect certain terms it desires to assume and reject others; it must assume cum onere. N.L.R.B. v. Bildisco and Bildisco, 465 U.S. 513, 532 (1984). See also Richmond Leasing Co. v. Capital Bank, 762 F.2d 1303, 1311 (5th Cir. 1985); City of Covington v. Covington Landing Limited Partnership, 71 F.3d 1221, 1226 (6th Cir. 1995) (Neither the debtor nor the bankruptcy court may excise material obligations owing to the non-debtor contracting party.); In re S.E. Nichols Inc., 120 B.R. 745, 747 (Bankr. S.D.N.Y. 1990) ("It is well-settled that a debtor cannot assume part of an unexpired lease while rejecting another part; the debtor must assume the lease *in toto* with both the benefits and burdens intact.").

It is illogical that the same principle would not apply pre-assumption. Surely, Congress did not intend that a debtor would be accorded the right to revise a contract prior to assuming it when it is not permitted to do so after assumption.

Under the guise of fostering reorganization, the Ninth Circuit has created a rule of law which has no conceptual support in any other facet of bankruptcy law. Judge Russell pinpointed the ramifications of such a result:

> Upon close scrutiny, those cases represent judges 'legislating' a result with no basis under §365, in order to achieve a result which those courts felt would better serve some bankruptcy purpose. As the majority states: 'This policy also balances the contract rights of the landlord, while protecting the debtor's rights to the §365 period under which to decide whether to assume or reject the lease.' In my opinion, the balancing act is an improper taking of the lessor's bargained for contractual rights. 190 B.R. at 380.

C. The Ninth Circuit Has Violated the "Plain Meaning" Rule

This Court has held that the "plain meaning of legislation should be conclusive, except in 'rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters." U.S. v. Ron Pair Enterprises, Inc., 489 U.S. 235, 242 (1989), quoting Griffin v. Oceanic Contractors, Inc., 458 U.S. 569, 571 (1982); See also Patterson v. Shumate, 504 U.S. 753, 761 (1992). The Ninth Circuit has given no credence to the unequivocal language of §365 (d)(3) which requires debtors to abide by their post-petition lease obligations prior to assumption or rejection.

Section 365 (d)(3) provides that:

> The trustee shall timely perform all the obligations of the debtor, except those specified in §365 (b)(2), arising from and after the order for relief under any unexpired lease of non-residential real property, until such lease is assumed or rejected, notwithstanding §503 (b)(1) of the this title . . . (emphasis added).

In holding that the renewal option could be exercised, notwithstanding the existence of an uncured default, the Ninth Circuit reached an interpretation of §365 which defies the clear language of the statute. The requirement to "timely perform all obligations" arising after the bankruptcy filing is absolute, and the Ninth Circuit had no statutory basis for eliminating the Debtors' burden to fulfill all conditions precedent to the exercise of its option to renew the Coleman leases. See In re M.S. Freight Distribution, Inc., 172 B.R. 976, 979 (Bankr. W.D. Wa.) ("This court therefore concludes that 'all obligations' means just that.").

Section 365(d)(3) was enacted in 1984 "to ameliorate the immediate financial burden borne by lessors of nonresidential property during the period in which trustees decided whether to assume a lease." In re Pacific-Atlantic Trading Co., 27 F.3d 401, 403 (9th Cir. 1994). See also In re Handy Andy Home Improvement Centers, Inc., 196 B.R. 87, 95 (Bankr.N.D.Ill. 1996), aff'd, 1997 WL 619824 (1997)); In re Paul Harris Stores, Inc., 148 B.R. 307, 313-14 (S.D.Ind. 1992). The legislative history for this provision fully supports this conclusion.

> [T]he landlord is forced to provide current services — the use of its property, utilities, security, and other services — without current payment. No other creditor is put in this

> position. In addition, the other tenants often must increase their common area charge payments to compensate for the trustee's failure to make the required payments for the debtor. The bill would lessen these problems by requiring the trustee to perform all the obligations of the debtor under a lease of nonresidential real property at the time required in the lease. (Emphasis added).
>
> H.R.Rep. No. 882, 95th Cong., 2d Sess.1984, reprinted in 1984 U.S. Code Cong. & Ad. News 576.

This congressional intent and the language of the statute are in accord; the purpose of §365(d)(3) is to protect the landlord who is bound to a pre-petition lease by requiring the debtor to abide by the requirements of the lease until it is assumed or rejected. See In re Handy Andy Home Improvement Centers, Inc., 196 B.R. at 95.

In this case, the Ninth Circuit ignored the precise mandate of §365(d)(3) in ruling that the Debtors could exercise the renewal option without meeting the post-petition conditions for extending the lease term. Under the clear language of the statute, these were obligations that had to be timely performed — the price, according to Congress, paid by the debtor to a landlord forced against its will to provide preassumption services.

In reaching its decision, the court below relied upon the reasoning of In re Webster Clothes, Inc., 36 B.R. 260, 1263 (D.Md. 1984), and that court's conclusion that the goal of §365 is "the preservation of the status quo until the debtor-in-possession decides whether to assume or reject." Significantly, Webster was decided prior to the 1984 amendments to the Bankruptcy Code. If the Ninth Circuit

had followed the plain language of §365(d)(3) as passed by the 1984 amendments, the preservation of the status quo would have required strict compliance with lease provisions, including the requirement that all defaults be cured prior to the exercise of any renewal options.

For whatever reason, the Ninth Circuit was unduly concerned with the notion that requiring the Debtors to cure their defaults prior to exercising the renewal option had the practical effect of forcing an early decision to assume or reject. But this concern has no place in a proper analysis of §365(d)(3). For example, if the Debtors had failed to meet the notice precondition to exercising the option as opposed to the cure requirement, it is doubtful that the court's analysis would have become so strained. If the Debtors had simply failed to give timely notice of an intent to renew, it is fairly clear that the lease option would have expired because the Debtors would have failed to meet a contractual obligation. See In Re Crabb, 48 B.R. 165 (Bankr. D. Mass. 1985) (court refused to revive an expired lease because the debtor failed post-petition to give proper notice electing to exercise an option to extend). There is simply no reason to reach a different result simply because the Debtor's default involved an uncured prior breach rather than the failure to give a required notice.

D. The Ninth Circuit's Ruling Has A Broad And Negative Impact On The Commercial Marketplace.

The Ninth Circuit failed to take into account the devastating effects that its decision will have on future commercial transactions. The majority wrote: "Thus no principle of bankruptcy or contract law precludes us from permitting the Debtors here to extend their leases in a manner contrary to the leases' terms, when to do so will effectuate the purposes of section 365." 127 F.3d at 911. This statement imposes no limitation on the types of modifications that can be made to reduce the burden on a debtor wishing to assume an executory contract. Under this analysis, nothing would prevent a bankruptcy court from adjusting the amount of rent, eliminating a notice requirement, or lengthening the

contract term indefinitely. Any modification supposedly furthering reorganization would be justifiable.

Neither §365 nor any other provision of the Bankruptcy Code contemplates that non-debtor parties can be compelled essentially to enter into new agreements on terms for which they did not bargain and over which they had no control. As this Court has stated, "the highest public policy is found in the enforcement of the contract which was actually made." Santa Fe, Prescott, and Phoenix Railway Co. v. Grant Bros. Construction Co., 228 U.S. 177, 188 (1913). Certiorari is warranted in order to address an issue which has a potentially disastrous impact on commercial law.

CONCLUSION

In the past, the United States Supreme Court has granted petitions for review of decisions involving statutory construction or application based upon the significance of the issue in the administration of a statute. See States v. Ruzicka, 329 U.S. 287 (1946). Review has also been granted when the issue under review may impact other facets of society or when the case involves a matter of public interest. See National Boiler Mktg. Ass'n v. United States, 436 U.S. 816, 820 (1978); Rice v. Sioux City Cemetery, 349 U.S. 70, 79 (1955). Such considerations are clearly present in the instant case.

Based on the foregoing, Petitioner respectfully requests that the United States Supreme Court accept its Petition for Writ of Certiorari in order to address the proper interpretation of 11 U.S.C. §365 and that it reverse the Opinion of the Ninth Circuit Court of Appeals in this case.

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APPENDIX

Order of the United States Bankruptcy Court for the District of Arizona entered April 6, 1994 ..... 1a

Opinion and Amended Opinion of the United States Bankruptcy Appellate Panel of the Ninth Circuit filed December 11, 1995 and Amended January 8, 1996 ..... 9a

Opinion of the United States Court of Appeals for the Ninth Circuit filed October 22, 1997..... 43a

Bankruptcy Code, Section 365 (11 U.S.C. § 365) 60a

FILED
APR 06 1994
KEVIN E. O'BRIEN CLERK
UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

UNITED STATES BANKRUPTCY
DISTRICT OF ARIZONA

In re	)	Chapter 11
	)	
THE CIRCLE K	)	Nos. B-90-5052-PHX-GBN
CORPORATION;	)	to B-90-5075-PHX-GBN
CIRCLE K	)	
CONVENIENCE	)	(Jointly Administered)
STORES, INC.;	)	
CIRCLE K	)	
MANAGEMENT	)	
COMPANY; LAR-LIN,	)	
INC.; FIRST CIRCLE	)	
PROPERTIES, INC.;	)	
UTOTEM, INC.;	)	
UTOTEM MARKETS	)	
OF ARIZONA, INC.;	)	
U TOTEM OF	)	
ALABAMA, INC.;	)	
U-TOTE'M OF	)	
COLORADO INC.;	)	
U-TOTE'M OF	)	
MIAMI, INC.; TIC	)	
TOC SYSTEMS,	)	
INC.; MONTERRE	)	
PROPERTIES, INC.;	)	
SHOP & GO, INC.;	)	

CIRCLE K GENERAL, INC.; CIRCLE K HAWAII, INC.; COMBINED AVIATION CO.; CHARTER MARKETING COMPANY (CONNECTICUT); CHARTER MARKETING COMPANY; MR. B'S OIL CO., INC.; MR. B'S FOOD MART INC.; NPI CORPORATION; OLD COLONY PETROLEUM) COMPANY, INC.; NEW ENGLAND PETROLEUM DISTRIBUTORS, INC.; and 44TH STREET & CAMELBACK LIMITED PARTNERSHIP, Debtors.	)	
COLEMAN OIL COMPANY, INC., a New Hampshire corporation, Plaintiff,	)	Adversary no. 91-974-GBN

vs.	)	ORDER
THE CIRCLE K CORPORATION, et al.	)	
Defendants.	)	

This matter is before the Court on debtors' Motion for Summary Judgment (Adversary Docket No. 51).

Upon consideration of the papers filed in this adversary proceeding, including documentary and affidavit testimony as to the chain of name changes, mergers, liquidation of subsidiary into parent corporations and assignments by which debtors New England Petroleum Distributors, Inc. and Old Colony Petroleum, Inc., now known as The Circle K Corporation, claim to be the current assignees and holders of the leasehold interests described in paragraphs 1 and 2 below, and upon consideration of oral argument on March 17, 1994, and of the interests of creditors and the estates, this Court finds and concludes that the debtors New England Petroleum Distributors, Inc. and Old Colony Petroleum, Inc. were the assignees and holders of the leasehold interests and properly exercised their rights as assignees to renew the leases of Stores 2604, 2605, 84802, 84803, 84804, 84805 ("Subject Stores") in 1987 and 1992; the leases have not been nor are they now terminated; there is no genuine issue of material fact and debtors' Motion For Summary Judgment should be granted as a matter of law.

Detailed findings of fact and conclusions of law were made in the Court's ruling from the bench on March 17, 1994,

IT IS ORDERED, ADJUDGED AND DECREED as follows:

1. Pursuant to the confirmed Plan of Reorganization, Old Colony Petroleum Company, Inc. was merged into Circle K Convenience Stores, Inc. on July 23, 1993; on July 26, 1993, The Circle K Corporation merged into Circle K Convenience Stores, Inc.; in connection with that merger Circle K Convenience Stores, Inc. changed its name to The Circle K Corporation. The corporation now known as The Circle K Corporation is the current assignee and holder of the lessee's interest in the leaseholds granted by Coleman Oil, Inc. ("COC") as lessor to Pickering Oil Heat, Inc. as lessee pursuant to documents dated November 21, 1977, in:

Circle K Store No.:	Address:	Description
2604	2975 Lafayette Rd. Portsmouth, NH	Exhibit A hereto incorporated herein
2605	#7 Old Dover Rd. Durham, NH	Exhibit B hereto incorporated herein

2. New England Petroleum Distributors, Inc. is the current assignee and holder of the lessee's interest in the leaseholds granted by Coleman Oil, Inc. as lessor to

Pickering Oil Heat, Inc. as lessee pursuant to documents dated November 21, 1977, in:

Circle K Store No.	Address:	Description:
84802	Rt. 16B Old Rochester Rd. Dover, NH	Exhibit C hereto incorporated herein
84803	Route 125 Epping, NH	Exhibit D hereto incorporated herein
84804	158 Front Street Exeter, NH	Exhibit E hereto incorporated herein
84805	Route 236 Kittery, Maine	Exhibit F hereto incorporated herein

3. Debtors' Motion for Summary Judgment is granted.

4. Plaintiff's objections are overruled and the debtors Fourth, Eighth and Ninth Motions to Assume Real Property Leases, Subleases and Attendant Contracts are hereby granted and approved to the extent the motions seek approval of assumption of the leases to Stores 2604, 2605, 84802, 84803, 84804 and 84805.

5. The only post-petition defaults alleged to exist concern only Store 2605 and total $190.96. Such defaults are de minimis. They cannot result in the avoidance of the

otherwise properly exercised renewals of the leases of the subject stores. Debtors are to retender this amount to plaintiff.

6. Debtors believe they have cured all pre-petition monetary defaults through the confirmed plan and by payment of tax reimbursements to COC. Debtors believe there are no defaults remaining to be cured with respect to the assumption of the leases of Stores 2604, 2605, 84802, 84803 or 84804. If plaintiff believes there remain defaults to be cured with respect to those stores, it shall provide to debtors and the Court a specific list of such defaults within 30 days from the entry of this order, in connection with a motion to require their cure.

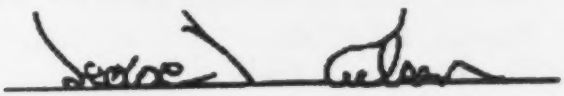
7. The Court shall retain jurisdiction over assumption of the Subject Stores to determine the existence of such defaults as may be specified by COC as provided in this order and their cure. Any pleadings directed to such defaults and their cure for purposes of debtors assumption shall be filed in the bankruptcy proceeding.

8. The adversary will be used by the Court to retain jurisdiction over cure of defaults in connection with assumption of the leases of the Subject Stores by debtors pursuant to 11 U.S.C. S 365(b).

9. This order resolves plaintiff's objection to the form of the order lodged by defendants.

10. The parties will appear for a status hearing, to last no longer than 15 minutes, on May 11, 1994, at 9:15 a.m., in Hearing Room No. 2, Fifth Floor, United States Courthouse, 230 North First Avenue, Phoenix, Arizona.

DATED this 6th day of April, 1994.



George B. Nielsen, Jr.
United States Bankruptcy Judge

Copy mailed the 6th day of April, 1994, to:

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ORDERED PUBLISHED

FILED DEC 11 1995
NANCY B. DICKERSON, CLERK
U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE NINTH CIRCUIT

In re	) BAP No. AZ-94-1422-JMeR
	)
THE CIRCLE K CORPORATION, et al.,	) BK. No. 90-5052-PHX-GBN to 90-5075-PHX-GBN
	)
Debtors.	) Adv. No. 91-974-GBN
	)
COLEMAN OIL COMPANY, INC., a New Hampshire corporation,	) **OPINION**
Appellant,	)
vs.	)
THE CIRCLE K CORPORATION, et al.,	)
Appellees.	)

Argued and Submitted on September 28, 1994
at Phoenix, Arizona

Filed - DEC 11 1995

Appeal from the United States Bankruptcy Court
for the District of Arizona

Honorable George B. Nielsen, Jr.,
Chief Bankruptcy Judge, Presiding

Before: JONES, MEYERS, and RUSSELL, Bankruptcy Judges.
JONES, Bankruptcy Judge:

A lessor leased nine gasoline service stations in New Hampshire and Maine to a lessee. The lease agreement was for ten years but could be renewed for two additional five-year periods. Through a series of mergers, acquisitions, and dissolutions, six of the stations ended up in the Circle K family of convenience stores.

Circle K declared bankruptcy and its subsidiaries gave notice that they intended to renew the leases even though the leases had not been assumed. Instead of moving to force Circle K to assume or reject under S 365(d)(2),[1] the lessor filed an adversary complaint arguing that the leases could not be renewed because (1) Circle K was not a proper assignee; (2) the leases were in default; and (3) the leases had not been assumed. Circle K moved for and was granted summary judgment. The lessor appeals. We **AFFIRM**.

I. FACTS

On November 21, 1977, Coleman Oil Company, Inc.

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[1]Unless otherwise indicated, all references to Chapters, Sections and Rules are to the Bankruptcy Code, 11 U.S.C. §§ 101, et seq. and to the Federal Rules of Bankruptcy Procedure, Rules 1001, et seq.

("Coleman") and Pickering Oil Heat, Inc. ("Pickering") entered into multiple ten-year lease agreements. The leases covered the following convenience store locations in Maine and New Hampshire: (1) Kittery; (2) Epping; (3) Exeter; (4) Dover; (5) Portsmouth; and (6) Durham. Paragraph 3 of the leases gave Pickering the following renewal rights:

> Lessee shall have two (2) additional and successive terms of five (5) years each on the same terms and conditions as during the original term (except there shall be no extension rights beyond the two contained in this paragraph), by giving Lessor at least six (6) months written notice of such extension prior to the expiration of the original or any extended term as the case may be, provided that Lessee's right to extend is conditioned upon the Lessee not being in default hereunder and is not in default of payments under any of the other leases described on Schedule C attached hereto.

The first option to renew the leases needed to be exercised on or about June 1, 1987. The second option to renew needed to be exercised on or about June 1, 1992.

NPI Corporation ("NPI") acquired Pickering's stock and other assets on December 31, 1983. NPI is the parent company of Debtor New England Petroleum Distributor ("New England") and Debtor Old Colony Petroleum, Inc. ("Old Colony"). New England claims that it is the valid holder of an assignment of the leases on the Kittery, Epping, Exeter, and Dover properties. Old Colony claims assignment of leases on the Portsmouth and Durham locations. NPI merged with

Charter International Oil Company ("Charter") on December 27, 1989. Circle K had previously acquired Charter on May 6, 1988, by purchasing all of its stock. During all of these transitions Coleman received and accepted the bargained for lease payments of $1,250 per month for each location.

On March 9, 1987, New England sent letters to Coleman exercising the option to renew the leases. On May 18, 1987, Old Colony also sent Coleman written notice that it was exercising its option to renew. Coleman did not object to the renewals, and continued to accept rent from both companies for the leased properties.

On May 15, 1989, Coleman informed its counsel that it might have to begin eviction proceedings, due to various defaults under the leases, unless New England and Old Colony could cure their defaults. Circle K, Old Colony, and New England, together with the rest of the Circle K family (collectively referred to as "Debtors"), filed for chapter 11 protection on May 15, 1990. The Debtors requested, and received, several orders during the bankruptcy proceedings granting extensions of time within which to assume or reject unexpired leases of nonresidential real property. See 11 U.S.C. § 365(d)(4) (1994) (requiring assumption of leases of nonresidential real property within 60 days of filing the petition unless an extension is granted by the bankruptcy court).

Coleman filed an adversary proceeding on October 11, 1991, seeking a declaration that Circle K was a tenant-at-will with no right to renew the leases, and also seeking relief from stay to terminate the leases. On March 5 and March 31, 1992, New England and Old Colony sent letters to Coleman exercising the option to renew for the second 5-year period.

The Debtors then moved for summary judgment in the adversary proceeding, asking the court to decide as a matter of law that (1) the Debtors were the legal assignees of the leaseholds and thus entitled to renew the leases; and (2) that the Debtors' renewal of the leases was effective even though the Debtors were in default in contravention of the lease's specific condition precedent. The bankruptcy court granted the motion for summary judgment on April 6, 1994. Coleman appeals.

II. ISSUES

1. Did the bankruptcy court err in holding as a matter of law that the Debtors are proper assignees of the Pickering lease?

2. Did the bankruptcy court err in holding as a matter of law that the Debtors could exercise their option to renew the leases even though the Debtors were in default, in contravention of the lease's specific condition precedent?

III. STANDARD OF REVIEW

We review a grant of summary judgment de novo. E.g., In re Hyman, 123 B.R. 342, 344 (9th Cir. BAP 1991), aff'd, 967 F.2d 1316 (9th Cir. 1992). On motion for summary judgment, the moving party has the burden to show that there are no genuine issues of material fact and therefore they are entitled to judgment as a matter of law. Celotex Corp. v. Catrett, 477 U.S. 317, 325 (1986).

IV. DISCUSSION

Coleman attacks the grant of summary judgment on

three fronts. First, Coleman argues that there are unresolved factual issues concerning the propriety of the Debtors' lease assignments which preclude a grant of summary judgment. Second, Coleman argues that the assignments are legally invalid under the statute of frauds because the assignments are not evidenced by a writing. Finally, Coleman argues that even assuming that the Debtors are valid assignees or successors, a chapter 11 debtor may not exercise an option to renew a lease unless the debtor first assumes the lease and cures any defaults. We address each of these arguments in turn.

A. Assignment of the Leases.

Coleman argues first that there are factual issues that must be resolved in order to determine whether the Debtors have a legal interest in the leasehold. Coleman points to the somewhat confusing series of mergers and acquisitions, the lack of written assignments to New England and Old Colony, and the lack of notice to Coleman of any purported assignments. The terms of the leases do not support these arguments.

The November 21, 1977 contract between Coleman and Pickering provides as follows:

> 11. Lessee shall have the right and privilege to assign this Lease or sublet said Premises in whole or in part, any extension thereof, upon such terms as to it shall seem best, PROVIDED, HOWEVER, that in the event of an assignment or sublet the Lessee shall remain primarily liable on said Lease.
>
> . . . .

> 22. The word "Lessor" herein shall be construed to include the said Lessor and Lessor's heirs, representatives, successors and assigns, as the case may be, and "Lessee" herein shall be construed to include the said Lessee, its successors and assigns.

The bankruptcy court interpreted this language as follows:

> The lease agreement itself specifically notes that the Lease is binding upon the parties and their successors and assigns. . . . The term Lessee itself is specifically construed to include successors and assigns.

The bankruptcy court found nothing in the contract to indicate that a formal assignment was required before a related entity could exercise the right to renew. The court also found nothing in the contract to indicate that Coleman required notice of assignments. The only requirement was that the original lessee, Pickering, would remain primarily liable under the lease. Finally, applicable Massachusetts law states that the surviving corporation of a merger or a consolidated corporation is vested with all right, title and interest in "all of the property, real, personal, or mixed" of the original corporation. Mass. Gen. L. Ch. 516 §§ 46(a)(4), (b), and (c) (1991).[2]

Having moved for summary judgment, the initial burden of showing an absence of any issues of material fact

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[2]Massachusetts is the state of incorporation of Old Colony, New England, NP Corp., NPI, and Pickering.

was upon the Debtors. We feel that the Debtors met their burden. The Debtors provided affidavits and documents concerning the numerous mergers, acquisitions and dissolutions. The bankruptcy court made the following conclusions:

> So in short, with respect to the Portsmouth and Durham stores, the chain of ownership of lessee's interest is as follows: Pickering to Pickering Old Colony, Inc., to Northeast Petroleum Corporation, to Old Colony Petroleum Company. With respect to the Epping, Exeter, Kittery and Dover stores, the chain of ownership in the lessee's interest is as follows: Pickering to Pickering Old Colony, Inc., to Northeast Petroleum Corporation, to New England Petroleum Distributors, Inc.

We agree with the bankruptcy court's conclusion that the documents presented by Debtors showed a chain of transfer of the subject leases.

Pursuant to Celotex, once the moving party has met its burden, the opposing party then has the burden to come forward with a more convincing showing that summary judgment is not appropriate. Celotex, 477 U.S. at 324. Coleman argues that the chain of assignment is too confusing to follow. Coleman also argues that there are holes in the paper trail presented by Debtors, and that Debtors' later behavior was inconsistent with the notion of an earlier assignment.

Coleman does not successfully argue that the chain of assignment is deficient as a matter of fact or that the contract

between Coleman and Pickering required documentation of assignments. Therefore, Coleman has failed to meet its burden pursuant to Celotex. We agree with the bankruptcy court's conclusion that no formal assignment of the leases or notice to the landlord was contemplated or required by the lease terms. Therefore, we affirm the bankruptcy court's decision that the Debtors were proper assignees of the lease, and therefore had the right to exercise the renewal option.

B. ***Applicability of the Statute of Frauds***

Coleman next attempts to raise a statute of frauds defense. It argues that a leasehold interest is subject to the statute of frauds and therefore the lease assignments at issue are invalid because they are not evidenced by a writing.

The bankruptcy court ruled that the statute of frauds was inapplicable because Coleman was not a party to the assignments. It concluded that third parties cannot assert the statute of frauds as a defense to an action by the direct parties to a contract because the statute of frauds is a shield, not a sword. Because the statute is intended to prevent fraud by one of the contracting parties on the other, if those parties recognize the contract, the protection afforded by the statute is unnecessary. Chapman v. Ford, 227 A.2d 26, 31 (Md. 1967)); see also Restatement (Second) of Contracts § 144 (1981) (stating that only a party to a contract or a transferee or successor of a party to the contract can assert that the contract is unenforceable under the statute of frauds).

We agree with this conclusion and therefore affirm the bankruptcy court's ruling that the statute of frauds is inapplicable in this case.

C. *Exercise of the Renewal Option in Bankruptcy*

Coleman next argues that the Debtors' attempt to exercise the renewal right for the final five-year option must fail because the Debtors were in default at the time they attempted to exercise the option to renew.[3] Coleman argues that the Debtors would have had to assume the lease and cure the defaults before they could exercise the right to renew. Since the Debtors failed to cure the defaults and assume the lease before the option period ran, the leases expired and there is nothing for the Debtors to now assume.

The heart of Coleman's argument against the Debtors' assumption of the leases lies in the conflict that often occurs between bankruptcy law and state law contract rights. Under paragraph 3 of the leases, a lessee could not exercise the option to renew a lease for another five-year period if the lessee was in default on the lease payments. At the time the Debtors attempted to exercise the option to renew, they were in default on the leases. It is therefore arguable that outside of bankruptcy, Coleman might have refused to accept the renewal unless the Debtors cured the minor defaults.[4]

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[3]The Debtors had defaulted both pre- and postpetition. While the exact amount and nature of the alleged defaults is unclear, the bankruptcy court characterized them as de minimis. The prepetition defaults apparently involved the failure by the Debtors to maintain the Kittery property in good repair and to pay property taxes in the amount of $4,470 on the Durham and Portsmouth stores. All postpetition property taxes were paid before Circle K exercised the options to renew, and the bankruptcy court stated that the amount of postpetition defaults existing at the time of renewal were alleged to be less than $200.

[4]It is by no means certain that outside of bankruptcy Coleman could have refused to accept the Debtor's attempt to exercise their option to renew. As the dissent points out, state anti-forfeiture law may have

The dissent argues that the same result should occur in bankruptcy; i.e., that the Debtors should be required to cure all pre- and postpetition defaults, no matter how small, in the time specified within the leases in order to exercise their option to renew. We disagree, and for the reasons discussed below hold that a debtor who is a lessee under a lease which conditions renewal upon not being in default may exercise its option to renew without first curing the default or assuming the lease.

1. Section 365(d)

The current version of § 365(d)(2) states that in a case under chapter 11, a trustee may assume or reject an unexpired lease of residential real property at any time before confirmation of the plan, unless the landlord asks for, and receives, a court order forcing the trustee to assume or reject the lease within a specified period. 11 U.S.C. § 365(d)(2) (1994). Section 365(d)(4) states that a trustee must assume an unexpired lease of nonresidential real property within 60 days of filing the petition, unless the trustee asks for a longer period of time. 11 U.S.C. § 365(d)(4) (1994).

Prior to the Bankruptcy Amendments and Federal Judgeship Act of 1984 ("BAFJA"), however, § 365 did not create a distinction between residential and nonresidential leases of real property.[5] In both cases a chapter 11 debtor in

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prevented Coleman from refusing to allow Circle K to renew the leases due to the de minimis nature of the defaults.

[5]BAFJA amended § 365(d) by adding § 365(d)(2), which required assumption or rejection of an unexpired lease of nonresidential real property within 60 days after the order for relief. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 362, 98 Stat. 333, 361 (1984); 2 Lawrence P. King, Collier on Bankruptcy, ¶ 365.03 at 365-24 n.1 (15th ed. 1995).

possession had until plan confirmation to decide whether to accept or reject an unexpired lease of real property, subject only to the landlord's right to ask the bankruptcy court to shorten that period. In pre-BAFJA decisions, therefore, landlords often brought motions to have the assumption/rejection period shortened. Some of these decisions involved situations similar to the instant appeal--an attempt by a debtor to exercise a option to renew an unexpired lease before actually assuming the lease and curing any defaults. Because the landlord had to come into court in order to shorten the assumption/rejection period, these decisions created a rule that turned on whether or not the landlord had asserted that "right."

This rule was first enunciated in In re Webster Clothes, Inc., 36 B.R. 260 (Bankr. D. Md. 1984). In Webster, the bankruptcy court allowed a debtor to exercise his option to renew an unexpired lease even though the debtor had defaulted prepetition. The court based its holding on various factors, including a statement that "[h]aving failed to avail itself of the statutory procedure for securing an earlier assumption or rejection of the lease, [the landlord] will not be heard to complain that [the debtor] had not assumed the lease at the time it exercised the Option."[6] Id. at 264.

The rule was also applied in In re Cook United Inc., 53 B.R. 342 (Bankr. N.D. Ohio 1985). In Cook United, the landlord had requested, and received, a court order forcing the debtor to assume or reject the unexpired lease within 60 days. For that reason the court held that the debtor could not renew

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[6]The other determining factors were that (1) section 365 governed the cure of defaults in unexpired leases; (2) the prepetition defaults were minor; and (3) the landlord had demonstrated no compensable, pecuniary loss resulting from the debtor's default. Webster, 36 B.R. at 264.

the lease unless it first assumed the lease and cured all defaults. Id. at 345. The court's opinion, however, clearly indicates that until a landlord files a motion asking the court to force the debtor to assume or reject the leases, "the federal policy to allow the debtor time to decide whether or not it will promptly cure a default outweighs state law contract provisions to the contrary." Id.

A similar situation also arose in In re Revco D.S., Inc., 111 B.R. 626 (Bankr. N.D. Ohio 1989). Although Revco arose after the BAFJA amendments, the debtor requested, and received, an order extending the period for assuming the lease until plan confirmation. Applying the Webster analysis, the court held that the debtor could "exercise its right to renew the Lease without assuming the Lease and curing the prepetition [default]," id. at 630, because the landlord had not "requested the Court to order debtor to assume or reject within a specified period of time." Id. at 629.

We agree with the reasoning of the above cases. However, given the current version of § 365 which places the burden on the debtor to seek an extension of time within which to assume or reject an unexpired lease of nonresidential property, we decline to base our decision on whether or not the landlord has sought a court order compelling the debtor to assume or reject within a specified time. Instead, we hold simply that a debtor who has defaulted prepetition on an unexpired lease may exercise its option to renew that lease without first assuming the lease or curing any prepetition defaults. Of course, such exercise must be conditioned upon the eventual assumption of the lease within the applicable time period and cure of all defaults in compliance with the requirements of § 365(b)(1).

The policy behind the Bankruptcy Code supports such a rule of law. The purpose behind S 365 is to balance the state law contract right of the creditor to receive the benefit of his bargain with the federal law equitable right of the debtor to have an opportunity to reorganize. See Webster, 36 B.R. at 263. This is accomplished by forcing the debtor to abide by the contract provisions during pendency of the bankruptcy and cure any prepetition defaults upon assumption while prohibiting the creditor from enforcing any prepetition default remedies. 11 U.S.C. §§ 365(b)(1), 365(d)(3), 362(a)(3) (1994). This balance, we believe, allows a debtor to exercise an option to renew an unexpired lease without first curing any prepetition defaults.[7] Coleman will receive the benefit of its bargain when, on assumption of the leases, Debtors are required to cure all pre- and postpetition defaults.

The dissent initially states that no other court has ever stated the rule of law which we adopt in this decision. However, as the above discussion demonstrates, our decision is supported by Revco, Cook, and Webster. The dissent disagrees with the holdings of these cases by concluding that they "represent judges 'legislating' a result" with no statutory authority. We decline to accept that characterization of these holdings, preferring to instead to view them as proper exercise of a bankruptcy court's authority to interpret the Bankruptcy Code in situations where the Code does not clearly resolve an issue.

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[7] As previously cited cases have illustrated, the lessor may prevent this occurrence by moving the bankruptcy court to force the debtor to assume or reject the unexpired lease before the option period expires.

The dissent quotes one statement from Cook United for what it believes is the correct view of this issue--that a bankruptcy court "has no authority to modify or nullify contractual provisions." Cook United, 53 B.R. at 345. However, the bankruptcy court in Cook United cited In the Matter of Schokbeton Indus. Inc., 466 F.2d 171 5th Cir. 1972), as authority for this proposition. As the following discussion indicates, the reasoning behind Schokbeton is clearly inapplicable.

Schokbeton was a case decided during an "arrangement proceeding" under Chapter XI of the Bankruptcy Act and which concerned the termination of a franchise agreement. There was no automatic stay in Chapter XI arrangement proceedings; instead, § 314 gave the court discretion to enjoin or stay the commencement or continuation of any suits against property of the debtor and to enjoin or stay any act to enforce any lien against property of the debtor. Bankruptcy Act of 1898, 30 Stat. 544 (1898) (as amended by the Chandler Act, Pub. L. No. 75-696, S 314, 52 Stat. 840, 907 (1938)), repealed by Bankruptcy Reform Act of 1978, Pub. L. No. 98598, § 401, 92 Stat. 2549, 2682 (1978). In Schokbeton, the franchise agreement provided for a 60-day grace period to cure any default in royalty payments. The franchisee did default and the franchisor notified him that he had 60 days in which to cure. Before the expiration of the 60 days, the franchisee filed a petition under Chapter XI of the Bankruptcy Act. Notwithstanding the bankruptcy filing, the franchisor terminated the franchise after the 60 days expired. The franchisee then petitioned the bankruptcy referee to enjoin the franchisor from granting the exclusive franchise to another licensee. Schokbeton, 466 F.2d at 173-74. After the referee granted the injunction, the franchisor appealed.

The Fifth Circuit reversed, holding that under the Bankruptcy Act "a contractual termination provision is unaffected by the filing of a petition in bankruptcy and may be enforced against the trustee or debtor in possession." Id. at 176. The court also noted that under the Bankruptcy Act a contract or lease provision which stated that filing a bankruptcy petition automatically terminated the lease was valid and could not be enjoined by a bankruptcy referee. Id. This decision, and the rationale behind it, is clearly not applicable under the Bankruptcy Code. Cook United, 53 B.R. at 345; 11 U.S.C. § 365(e)(1)(B) (1994) (preventing enforcement of any clause in an executory contract or unexpired lease which purports t terminate the agreement if one party files for bankruptcy).

We are also concerned with the leverage landlords would receive if debtors were forced to cure prepetition defaults before deciding whether or not to assume a lease. Bankruptcy Code § 365(b)(1) requires a debtor to cure or provide adequate assurances that it will promptly cure prepetition defaults at the time it assumes or rejects a contract. 11 U.S.C. § 365(b)(1) (1994). If a debtor does not assume a contract or unexpired lease, the existing default becomes an unsecured claim and is paid with no more priority than any other unsecured creditor enjoys under the Code. E.g., In re Pacific Express Inc., 780 F.2d 1482, 1486 (9th Cir. 1986). A debtor in possession can assume or reject an executory contract or unexpired lease of residential real property at any time before plan confirmation. 11 U.S.C. S 365(d)(2) (1994). Although an unexpired lease of nonresidential real property must be assumed or rejected within 60 days of filing the petition, 11 U.S.C. § 365(d)(4) (1994), debtors are often granted extensions of time well beyond this 60-day period.

Under the dissent's rationale, a lessor could force a debtor to cure prepetition defaults in order to preserve its right to exercise a renewal option. If the lease is ultimately rejected, however, the prepetition default would have been a general unsecured claim. In effect, the lessor is given leverage to squeeze a preference out of the debtor. We do not feel this result is in line with the policy behind the Bankruptcy Code in general or behind § 365 specifically.

The dissent disagrees with this analysis, stating that the lessor's exercise of its "lawfully bargained for rights" in this situation is not unfair "leverage," but merely enforcement of its contract rights. The dissent characterizes our holding as a "balancing act [which] is an improper taking of the lessor's bargained for contractual rights." This view is at odds with both the plain language and purposes of the Bankruptcy Code, which in various ways nullifies, modifies or stays creditors' lawfully bargained for contract rights. E.g., 11 U.S.C. §§ 362, 365, 522(f), 524, 544, 545 (1994). If the dissent's theory were correct, then any landlord could defeat § 365 by inserting a lease provision that requires a complete cure of any defaults before exercising an option in the lease. Surely the Bankruptcy Code was not intended to allow such circumvention. E.g., 365(e)(1)(B) (1994).

2. Section 108

The dissent fails to cite a single case in support of its position that a debtor must cure all prepetition defaults before exercising an option to renew which is conditioned upon the debtor not being in default. Instead, the dissent points to § 108(b). Section 108(b) states that if state law or an agreement fixes a certain period in which the debtor may cure any defaults, and the default period has not yet expired at the time

of filing bankruptcy, the debtor has until the later of the end of the period contained in the agreement or 60 days after the bankruptcy petition is filed.

We disagree with this analysis, finding more persuasive the reasoning behind the decision in Moody v. Amoco Oil Co., 734 F.2d 1200 (7th Cir.), cert. denied, 469 U.S. 982 (1984). [8] In Moody, a jobbership contract between the debtor and a creditor provided for a fifteen day cure period after a default. The debtor defaulted, then filed bankruptcy before expiration of the fifteen day cure period. The creditor, referring to § 108(b), argued that the debtor had to cure its default within 60 days or the jobbership contract would terminate. The court disagreed, holding that "section 108(b) does not apply to curing defaults in executory contracts" because "[s]ection 365 specifically governs. . . ." Id. at 1215; accord, In re McCallen, 49 B.R. 948, 952 (Bankr. D. Or. 1985).[9]

The dissent argues that the rationale behind Moody is not applicable to the instant appeal, because "[a]lthough § 365

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[8] Although the Moody decision specifically concerned executory contracts, its reasoning is just as applicable to unexpired leases.

[9] Moody, the Seventh Circuit distinguished the case of Johnson v. First Nat'l Bank of Montevideo, 719 F.2d 270 (8th Cir. 1983), cert. denied, 465 U.S. 1012 (1984), which held that § 108(b), rather than § 362, governed the expiration of a statutory period of redemption of a mortgage. The court in Moody explained that § 362 does not specifically apply to redemption periods and therefore there was no direct conflict between those two provisions. However, there is a direct conflict between § 108(b) and S 365 as applied to executory contracts (and unexpired leases), and therefore these two sections "should not [be] appl[ied] . . . so as to cause irreconcilable conflict. . . ." Moody, 734 F.2d at 1215 n.15.

may extend the time for curing defaults until assumption of the lease, it does not eliminate the contractual necessity of not being in default when attempting to exercise the options to extend the leases." However, the dissent fails to cite any statutory or case authority for this distinction. We think the policy considerations outlined in Moody are applicable in the instant appeal:

> This holding is consistent with the policies underlying the different provisions and the Code in general. The purpose behind section 108(b) is to permit the debtor an extension of time for doing certain acts necessary to preserve his rights. It would be anomalous to apply it to restrict debtor's rights . . . . Applying section 108(b) here would force debtors to decide whether to cure long before they must decide whether to assume or reject the contract and long before they know whether any reorganization plan will be confirmed. Finally, the purpose behind chapter 11 is "to permit successful rehabilitation of debtors" and "to prevent a debtor from going into liquidation." Debtors must be permitted a certain amount of flexibility in determining whether to assume or to reject a contract. Specific provisions of the Code should be interpreted with this goal in mind. To interpret the Code so as to minimize flexibility and rush the debtor into what may be an improvident decision does not further the purposes of the reorganization provisions.

Moody, 734 F.2d at 1216 (citation omitted).

D. Alternative State law Theory

Responding to Coleman's argument that the leases had terminated prepetition due to the invalidity of the lease assignments, the bankruptcy court supported its grant of summary judgment by applying the Ninth Circuit opinion in In re Waterkist Corp., 775 F.2d 1089, 1091 (9th Cir. 1985). Waterkist presents a two-part analysis, first asking whether the lease-was terminated prepetition pursuant to the contract under applicable state law and, if so, asking whether the termination would have been reversed under state anti-forfeiture provisions. We decline to address this issue, however, because the Waterkist analysis requires the balancing of equities between lessor and lessee in order to decide whether state anti-forfeiture provisions would prevent termination of a lease. This determination requires findings of fact inappropriate on a motion for summary judgment.

V. CONCLUSION

Coleman challenges the chain of assignment between Pickering and Debtors, but fails to meet its burden under Celotex. Having failed to raise material issues of fact, Coleman raises the statute of frauds as an issue of law. However, Coleman lacks standing to raise this legal argument because it was not a party to the assignment contract. Finally, § 365(d) permits a debtor to exercise an option to renew an unexpired lease prior to assumption and cure. Accordingly, the order granting summary judgment is **AFFIRMED**.

RUSSELL, Bankruptcy Judge, dissenting:

I respectfully dissent.

Although I agree with the majority that the debtors in possession are proper assignees of the leases, I cannot agree that the leases were properly assumed. I agree with Coleman's argument that the attempt by the debtors in possession to exercise the extension rights for the final five-year option must fail because the debtors in possession were in default both pre- and postpetition.

The issue before us is not whether the debtors in possession can exercise their options to renew the six leases without assuming the leases and curing the defaults. [10] Rather, the issue before us is whether the options could have been exercised without first curing the defaults. If not, then there were no leases for the debtors in possession to later assume.

Paragraph 3 of the leases provides that the lessee could exercise the extension rights:

> [B]y giving Lessor at least six (6) months written notice of such extension prior to the expiration of the original or any extended term as the case may be, Provided that Lessee's right to extend is conditioned upon the Lessee not being in default hereunder and is not in default of payments under any of the other leases described on Schedule C attached hereto. (Emphasis added.)

The debtors in possession filed their bankruptcy cases on May 15, 1990. Under the leases, the first extension of the

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[10] However, if this were the issue, I would hold that in order to exercise their options to extend the six leases, the debtors in possession must assume the leases and perforce cure the defaults.

leases would have expired on November 20, 1992, unless the written notices to renew were given by May 20, 1992. Although the written notices were sent, the leases were in default at that time.

I know of no provision in the Bankruptcy Code which gives a debtor in possession the right to exercise an option without also curing any default as required by the very contract which gives the lessee the right to exercise the option. Although the majority argues that § 365 abrogates an important right of the lessor in the lease, i.e., the right to have all defaults cured when the option is exercised, they point to no specific part of § 365 to achieve this result.

There is nothing in § 365 that extends the time to exercise the option and the fulfillment of any conditions precedent, such as not being in default, at the time of the purported exercise. Since the time to exercise the options expired, the leases were terminated.

It is clear that the notice required to exercise the option was not extended pursuant to§ 108(b). [11] Therefore, pursuant

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[11] Section 108(b) provides:

> (b) Except as provided in subsection (a) of this section, if applicable nonbankruptcy law, an order entered in a nonbankruptcy proceeding, or an agreement fixes a period within which the debtor or an individual protected under section 1201 or 1301 of this title may file any pleading, demand, notice, or proof of claim or loss, cure a default, or perform any other similar act, and such period has not expired before the date of the filing of the petition, the trustee may only file, cure, or perform, as the case may be, before the later of -

to ¶3 of the leases, the debtors in possession were required to timely exercise the options. Indeed, the debtors in possession recognized the need to timely exercise the options by attempting to do so. However, a condition precedent for the right to exercise the options was not being in default on the leases. Since the defaults were not cured, there was no timely exercise of the options. Thus, the leases were terminated.

The majority states its holding as follows:

> We disagree [with the dissent] and for the reasons discussed below hold that a debtor who is a lessee under a lease which conditions renewal upon not being in default may exercise its option to renew without first curing the default or assuming the lease.

Unfortunately for the majority, no other court, at least none of those cited by the majority, has ever stated such a rule of law.

The majority relies on a number of bankruptcy court decisions, mainly, In re Revco D.S., Inc., 111 B.R. 626 (Bankr. N.D. Ohio 1989), In re Webster Clothes, Inc., 36 B.R. 260 (Bankr. D. Md. 1984), In re Cook United, Inc., 53 B.R. 342 (Bankr. N.D. Ohio ,985) and In re Tirenational Corp., 4i B.R. 647 (Bankr. N.D. Ohio 1985).

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(1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or

(2) 60 days after the order for relief. 11 U.S.C. § 108(b) (emphasis added).

Upon close scrutiny, those cases represent judges "legislating" a result with no basis under § 365, in order to achieve a result which those courts felt would better serve some bankruptcy purpose. As the majority states: "This policy also balances the contract rights of the landlord, while protecting the debtor's rights to the § 365 period under which to decide whether to assume or reject the lease." In my opinion, the balancing act is an improper taking of the lessor's bargained for contractual rights.

The majority first notes that they "are concerned with the dissent's position would give to landlords". The then disagrees with my dissent as follows:

> Under the dissent's rationale, a lessor could force a debtor to cure prepetition defaults in order to preserve its rights to exercise a renewal option. If the lease is ultimately rejected, however, the prepetition default would have been a general unsecured claim. In effect, the lessor is given leverage to squeeze a preference out of the debtor. We do not feel this result is in line with the policy behind the Bankruptcy Code in general or behind § 365 specifically.

The majority has a very interesting way of looking at a lessor's contractual rights in a pejorative sense of giving "the lessor leverage to squeeze a preference out of the debtor". I suppose it is possible for a court to look at any party's exercise of its lawfully bargained for rights against a debtor in possession as unfair "leverage." However, I choose not to view parties' rights in this light.

Indeed, the court in Cook United, supra, stated what I believe is the law:

> Debtor is requesting this Court to rewrite the leases and Section 365 of the Bankruptcy Code, by holding that even though it was in default, Debtor had a right to exercise its option to renew the leases prior to its assuming said leases and curing the defaults. This Court cannot do so. The bankruptcy court has no authority to modify or nullify contractual provisions. Matter of Schokbeton Indus., Inc., 466 F.2d 171 (5th Cir. 1972).

53 B.R. at 345 (emphasis added).

Moody v. Amoco Oil Co., 734 F.2d 1200 (7th Cir.), *cert denied*, 469 U.S. 982 (1984), offers no support for the majority's holding. In relevant part, Moody merely stands for the proposition that § 108 does not generally apply to curing defaults in executory contracts, but that such time limit is governed by § 365.

Moody is of no assistance to the majority's reasoning because the time limit that is in question in the case before us is the period of time in which to timely exercise an option. Although § 365 may extend the time for curing defaults until assumption of the lease, it does not eliminate the contractual necessity of not being in default when attempting to exercise the options to extend the leases.

The facts in Revco were very similar to those in the case before us. While in default, the debtor in possession notified the lessor, postpetition, that it was exercising its

option to extend the lease. The court held that the debtor in possession could properly exercise the option to extend the lease, without assuming the lease and curing the default, because the lessor failed to request the court to order the debtor in possession to assume or reject the lease. Without any independent analysis, the court based its holding on the following cases: Cook United, supra; Tirenational, supra; and Webster, supra.

In Cook United, the court held that the option to extend the leases could not be exercised without the debtor in possession first assuming the leases and curing the defaults. Approximately one month prior to the date on which the debtor in possession was required to exercise the option under the leases, the lessor filed an application to require the debtor in possession to assume or reject the leases. The debtor in possession failed to assume or reject the leases prior to the expiration of the leases.

The holding of Cook United which is relevant to the matter before us was stated as follows:

> Once a request is made by the lessor to assume or reject, federal policy no longer overrides the contract, and the lease terms retain their original effect. Thus once Glimcher filed for an order to assume or reject, Debtor had to assume and cure all defaults before it could exercise the option to renew. This is especially so where the lease provision in question is an option to renew. Such provisions are designed to provide the lessor with enough time to find a new tenant if the lease is not renewed. To allow Debtor to exercise the option without assuming

> the lease would be a substantial interference with the contractual rights of the lessor, because he would not know if the lessee intended to remain, the very thing for which he bargained. Where the lessor has requested assumption or rejection, Debtor must assume before it may exercise an option to renew. In order for Debtor to reap the benefits of a contract, it must at the same time bear the burdens of that contract. In re Tirenational Corp., 47 B.R. 647 (Bankr. N.D. Ohio 1985).

53 B.R. at 345.

My only disagreement with the above statement by the court in Cook United is that I see no requirement in either bankruptcy or non-bankruptcy law that the lessor must first apply to the bankruptcy court to order the debtor in possession to assume or reject the lease before being entitled to the contractual benefits of the lease which the Cook United court stated it ". . . has no authority to modify or nullify. . . ." Id.

The only case authority cited by the court in Cook United for the purported rule of law is Tirenational, supra, which does not support this conclusion and which offers no support for the majority's position.

Tirenational involved two separate chapter 11 cases in which the debtor in possession in the first case was the franchisor and the debtor in possession in the second case was the franchisee. After the filing of the franchisor's case, but before the filing of the franchisee's case, the franchisee was in substantial default on its payments. Therefore, the franchisor notified the franchisee that the franchise agreement was

terminated.

The issue before the court was whether the franchisor could exercise its termination rights without first assuming the franchise agreement. If it could, then the agreement was terminated prior to the franchisee's filing its chapter 11 case and consequently would not be property of the franchisee's bankruptcy estate.

The court correctly held that until the agreement was assumed or rejected, it remained in effect and the franchisor/debtor in possession could exercise its termination rights against the franchisee. The case did not involve the exercise of an option to extend and did not involve any purported requirement that a lessor file a motion requiring a lessee to assume or reject the lease before the lessor could exercise its contractual rights.

Therefore, Tirenational is not relevant to the question before us, i.e., whether a debtor in possession can exercise an option in violation of the express terms of the lease requiring the lessee not to be in default at the time the option is exercised.

In Webster, supra, the debtor in possession filed an application for authority to assume an unexpired lease for retail premises located in a shopping center, including a five-year extension period provided in the lease.

The debtor in possession timely notified the lessor of its intention to extend the lease. The lessor refused to accept the extension because the debtor was in default and had not assumed the lease. As in the case before us, the lease provided that to extend the lease for a five-year period, it must not be in

default. The court held that the attempted extension was effective, the lease had not terminated under its own terms and the lease could be assumed.

The court then announced its ruling as follows:

> Having failed to avail itself of the statutory procedure [under § 365(d)(4)] for securing an earlier assumption or rejection of the lease, Forbes-Cohen [lessor] will not be heard to complain that Webster [debtor in possession] had not assumed the lease at the time it exercised the Option.

36 B.R. at 264.

Apparently, not completely satisfied with its newly announced rule, the court went on to note that the default was "minor." The court then concluded:

> As a court of equity, this Court is loathe to enforce a forfeiture of the Option on the basis of a minor default. Webster's effective exercise of the Option deprives Forbes-Cohen only of the chance to relet the Premises to another tenant at a higher rent, a windfall. To hold that Webster has not exercised the Option would be to deprive the estate of a valuable asset and frustrate the cure provisions of Section 365.

Id. (citation omitted).

Although there is no authority for the court under federal law to excuse even a "minor" default, there may very

well have been state anti-forfeiture laws which would allow the court to avoid a forfeiture. Indeed, as discussed below, I would reverse and remand the case before us for the bankruptcy court to make such a determination under state anti-forfeiture law.

It is clear from the record, as the majority concedes, that there were both pre- and postpetition defaults under the leases. The majority also concedes that the determination and the amount of the defaults was not appropriate on a motion for summary judgment.

Under state anti-forfeiture law, however, it may be possible for the debtors in possession to avoid the termination of the leases. Therefore, this matter should be reversed and remanded to the bankruptcy court in order to provide the debtors in possession the opportunity to have the bankruptcy court consider reviving the leases under state anti-forfeiture law.

CONCLUSION

The failure of the debtors in possession to cure all defaults at the time of their attempted exercise of the options, in violation of the specific requirement in the leases, resulted in the leases being terminated for failure to timely exercise the options. Nevertheless, it may be possible for the debtors in possession to revive the leases pursuant to state antiforfeiture law.

I would therefore REVERSE the bankruptcy court's granting of the motion for summary judgment by the debtors in possession, and REMAND the matter for the bankruptcy court to consider the possible revival of the leases under state anti-forfeiture law.

ORDERED PUBLISHED

FILED
Jan - 8 1996
Nancy B. Dickerson, Clerk
L.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re	) BAP No. AZ-94-1422-JMeR
	)
THE CIRCLE K	) BK. No. 90-5052-PHX-GBN
CORPORATION, et al.,	) to 90-5075-PHX-GBN
	)
Debtors.	) Adv. No. 91-974-GBN
	)
COLEMAN OIL	) **AMENDED**
COMPANY, INC.,	) **OPINION**
a New Hampshire	)
corporation,	)
Appellant.	)
vs.	)
	)
THE CIRCLE K	)
CORPORATION, et al.,	)
	)
Appellees.	)

Argued and Submitted on September 28, 1994
at Phoenix, Arizona

Opinion Filed - December 11, 1995
Amended Opinion Filed JAN - 8 1996

Appeal from the United States Bankruptcy Court
for the District of Arizona

Honorable George B. Nielsen, Jr.,
Chief Bankruptcy Judge, Presiding

Before: JONES, MEYERS, and RUSSELL, Bankruptcy Judges.

The dissent argues that the rationale behind Moody is not applicable to the instant appeal, because [a]lthough § 365 may extend the time for curing defaults until assumption of the lease, it does not eliminate the contractual necessity of not being in default when attempting to exercise the options to extend the leases. However, the dissent fails to cite any statutory or case authority for this distinction. We think the policy considerations outlined in Moody are applicable in the instant appeal:

> This holding is consistent with the policies underlying the different provisions and the Code in general. The purpose behind section 108(b) is to permit the debtor an extension of time for doing certain acts necessary to preserve his rights. It would be anomalous to apply it to restrict debtor's rights . . . . Applying section 108(b) here would force debtors to decide whether to cure long before they must decide whether to assume or reject the contract and long before they know whether any reorganization plan will be confirmed. Finally, the purpose behind

> chapter 11 is "to permit successful rehabilitation of debtors" and "to prevent a debtor from going into liquidation.. Debtors must be permitted a certain amount of flexibility in determining whether to assume or to reject a contract. Specific provisions of the Code should be interpreted with this goal in mind. To interpret the Code so a" to minimize flexibility and rush the debtor into what may be an improvident decision does not further the purposes of the reorganization provisions.

Moody, 734 F.2d at 1216 (citation omitted).

D. Alternative State law Theory

As discussed above, the bankruptcy court rejected Coleman's argument that the leases had automatically terminated pre- or postpetition because the Debtors were in default at the time they exercised the options to renew. The bankruptcy court then stated that even if it held that the leases had terminated, state antiforfeiture law would allow the debtors to reinstate the leases. The bankruptcy court cited In re Waterkist Corp., 775 F.2d 1089 (9th Cir. 1985), as support. Waterkist presents a two-part analysis for determining whether a debtor can reverse the prepetition termination of a lease and thereafter assume the lease in bankruptcy; Under the Waterkist analysis, a court first determines whether the lease was terminated prepetition pursuant to the contract under applicable state law and, if so, whether the termination would have been reversed under state anti-forfeiture provisions. The bankruptcy court

indicated that under this analysis, the Debtors would probably be entitled to assume the leases even if they had terminated. We decline to address the propriety of this fact-intensive analysis, however, because we have already affirmed the bankruptcy court's decision for the reasons expressed in Part IV, subsection C above.

V. CONCLUSION

Coleman challenges the chain of assignment between Pickering and Debtors, but fails to meet its burden under Celotex. Having failed to raise material issues of fact, Coleman raises the statute of frauds as an issue of law. However, Coleman lacks standing to raise this legal argument because it was not a party to the assignment contract. Finally, § 365(d) permits a debtor to exercise an option to renew an unexpired lease prior to assumption and cure. Accordingly' the order granting summary judgment is **AFFIRMED**.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: THE CIRCLE K CORPORATION; Circle K Convenience Stores, Inc.; Circle K. Management Company; Lar-Lin, Inc.; First Circle Properties, Inc.; Utotem, Inc.; Utotem Markets of Arizona, Inc.; U Totem of Alabama Inc.; U-Tote'M of Colorado Inc.; U-Tote-M of Miami, Inc.; Tic Toc Systems, Inc.; Monterre Properties Inc.; Shop & Go, Inc.; Circle K General, Inc.; Circle K Hawaii, Inc.; Combined Aviation Co.; Charter Marketing Company (Connecticut); Mr. B's Oil Co., Inc.; Mr. B's Food Mart, Inc.; NPI Corporation; Old Colony Petroleum Company, Inc.; New England Petroleum Distributors, Inc.; and 44th Street & Camelback Limited Partnership,

Debtors.

COLEMAN OIL COMPANY, INC.,

Appellant,

v.

THE CIRCLE K CORPORATION,

Appellee.

No. 96-15200

BAP No.
AZ 94-01422-JmeR

OPINION

Appeal from the Ninth Circuit
Bankruptcy Appellate Panel
Jones, Myers and Russell, Judges, Presiding

Argued and Submitted
March 10, 1997—San Francisco, California

Filed October 22, 1997

Before: Byron R. White,* Associate Justice, Retired,
William C. Canby and Pamela Ann Rymer, Circuit Judges.

Opinion by Judge Canby; Partial Concurrence and
Partial Dissent by Judge Rymer

SUMMARY

Bankruptcy/Real Estate

The court of appeals affirmed a judgment of the bankruptcy appellate panel (BAP). The court held that a lease provision barring the exercise of a renewal option by a lessee in default does not preclude a defaulting Chapter 11 bankruptcy debtor from doing so.

Appellant Coleman Oil Company leased gasoline stations to Pickering Oil Heat for ten years with options to renew for two additional five-year terms. The leases permitted renewal on six months notice if none of the leases was in default.

Two subsidiaries of appellee the Circle K Corporation (New England Petroleum Distributors and Old Colony Petroleum) assertedly acquired the lessees' interests. After one

*The Honorable Byron R. White, Retired Associate Justice of the United States Supreme Court, sitting by designation.

renewal of the leases in 1987, the subsidiaries defaulted on some of the lease provisions; they and Circle K sought Chapter 11 bankruptcy protection. They obtained an extension of time from the bankruptcy court to make their decision to assume or reject the leases until after the June 1992 expiration of the first renewals.

Coleman brought an adversary action, alleging that the debtors were merely tenants at will. Coleman contended that the debtors were not assignees of the leases because the assignments were defective and violated the statute of frauds. Alternatively, Coleman asserted that even if the assignments were valid, the lessees had failed to exercise the options properly, so that the leases had expired unrenewed.

In March 1992, Old Colony and New England notified Coleman that they had elected to extend the leases for another five years, even though the prepetition defaults had not been cured. In the adversary action, the debtors moved for summary judgment. The bankruptcy court granted the motion.

The BAP affirmed, concluding that Coleman had failed to raise a material issue of fact regarding the debtors' status as assignees; Coleman lacked standing to challenge the assignments under the statute of frauds; and the debtors successfully renewed the leases even though they were in default at the time of the second exercise. As did the bankruptcy court, the BAP based its ruling on the rationale underlying 11 U.S.C. § 365: to balance the state-law contract right of the creditor to receive the benefit of its bargain with the federal law equitable right of the debtors to an opportunity to reorganize.

Coleman appealed, reiterating its position in the bankruptcy court, and asserting that summary judgment was inappropriate because it had raised an issue of material fact: the debtors' actions (contemporaneous requests to extend some of the same leases) had been inconsistent with the assignments.

[1] New England's and Old Colony's inconsistent or mistaken behavior did not make the assignments ineffective. In the face of the debtors' uncontradicted evidence, such minimal evidence of equivocal behavior would have been insufficient for a reasonable jury to find that the assignments had not occurred. [2] Coleman's invocation of the statute of frauds was meritless. Merely because it was the lessor, Coleman was not a party to any of the assignments. The parties to the assignments did not challenge their validity. It would have been for them, not Coleman, to raise the statute of frauds as a defense to enforcement of the assignments, if they so chose.

[3] The extensions in 1987 were no longer open to challenge. All parties acted as if the extensions were effective, and any objections to them had long since been waived. Coleman accepted rent and otherwise treated the debtors as lessees for years after 1987. Coleman was estopped from asserting ten years later that the leases expired in 1987. The leases remained effective from 1987 to 1992.

[4] There were defaults under at least some of the leases. The exact nature and extent of the defaults was immaterial because the bankruptcy court had the power to permit the debtors to extend the leases without first curing the defaults.

[5] In conjunction with the automatic stay, § 365 suspends the termination of lease that is in default; it extends the debtor lessee's opportunity to cure any defaults until the debtor has the chance to decide whether to assume the lease. The lessor will get the benefit of the bargain on assumption, when the debtor must cure the default.

[6] The practical effect of requiring the debtors to cure prepetition defaults in order to extend the leases would have been to require an early decision whether to assume or reject them. The bankruptcy court was not compelled to require a course of action that would have made the extension illusory, thus

depriving the debtors of the opportunity to reorganize without burdening the estate with unexpired lease obligations.

[7] All kinds of interference with contractual rights occur in bankruptcy proceedings. No principle of bankruptcy or contract law precluded the courts from permitting the debtors to extend the leases in a manner contrary to the leases' terms, when to do so would effectuate the purposes of § 365. [8] The debtors could exercise their final option to renew the leases without first curing the defaults. Thus renewed, the leases did not expire in 1992, and the debtors could assume them, curing the defaults or giving assurance of prompt cure at that time.

Judge Rymer concurred in part and dissented in part, concluding that § 365 does not extend the time to exercise an option to renew a lease, or to meet conditions precedent to doing so.

COUNSEL

Carolyn Johnsen, Herbert, Schenk, Johnsen & Dake, Phoenix, Arizona, for the appellants.

James L. Rasmussen, Kemp, Smith, Duncan & Hammond, Albuquerque, New Mexico, for the appellees.

OPINION

CANBY, Circuit Judge:

This case presents the question whether a lessee debtor in bankruptcy, prior to deciding whether to accept or reject non-residential leases, may exercise an option to renew the leases even though the lessee debtor is in default and the leases specify that they may not be renewed if in default.

The Coleman Oil Company, as lessor, leased six gasoline stations in New Hampshire and Maine for ten years, with options to the lessee to renew for two additional five-year terms. Each lease permitted renewal only if none of the leases was in default.

Two subsidiaries of the Circle K Corporation claimed to have acquired the lessees' interests under the leases by a series of acquisitions and mergers. After one renewal of the leases, disputed here, Circle K and its subsidiaries filed a Chapter 11 petition in bankruptcy. The lessee subsidiaries ("the Debtors") then sought and received an extension of time within which to assume or reject the leases. *See* 11 U.S.C. § 365(d)(4)(1994). The first five-year extension of the leases was due to expire, however, prior to the time when the Debtors were required to accept or reject the leases. In order to protect their future choice to accept or reject, the Debtors exercised their option to extend the leases for a second five-year term, even though pre-petition defaults in at least some of the leases had not been cured.

The paramount question before us is whether the need to preserve the Debtors' rights under 11 U.S.C. § 365 to accept or reject the leases overcomes the leases' requirement that none of the leases be in default at the time of renewal. We conclude, as did the bankruptcy court and the Bankruptcy Appellate Panel ("BAP"), that the leases may be renewed despite the uncured defaults. We also reject other arguments raised by appellants, and accordingly affirm the judgment of the BAP.

I. BACKGROUND

In November 1977, Coleman, as lessor, and Pickering Oil Heat, as lessee, entered into six leases. The leases covered the following gasoline and convenience store locations in Maine and New Hampshire: (1) Kittery; (2) Epping; (3) Exeter; (4) Dover; (5) Portsmouth; and (6) Durham.

The leases provided for an initial term of ten years, and gave Pickering the right to renew for two additional five-year terms under certain conditions:

> Lessee shall have two (2) additional and successive terms of five (5) years each . . . by giving the Lessor at least six (6) months written notice of such extension prior to the expiration of the original or any extended term as the case may be, *provided that Lessee's right to extend is conditioned upon the Lessee not being in default hereunder and is not in default of payments under any of the other leases* . . . .

ER 5 Exh. A at 2 (emphasis added). Thus, for Pickering or its assignees to extend the leases to the maximum period, they were required to exercise the first option by June 1987, and the second by June 1992.

The Debtors assert that they acquired Pickering's interest in the leases through a series of corporate mergers and acquisitions. Northeast Petroleum Inc. ("NPI") is the parent corporation of New England Petroleum and Old Colony Petroleum. NPI acquired Pickering's stock in December 1983 and merged with Charter International Oil in December 1989. Circle K acquired Charter in 1988. Circle K thus became the parent of New England and Old Colony. New England claims to be the assignee of the Kittery, Epping, Exeter, and Dover leases. Old Colony claims to be the assignee of the Portsmouth and Durham leases.[1]

During all of these transitions, Coleman received and accepted the full lease payments every month for each of the leases.

[1]Under the Chapter 11 Plan of Reorganization, Old Colony and New England merged into the Circle K Corporation. Because that merger occurred after the final extension of the leases, we ignore it for purposes of this opinion.

In March 1987, New England notified Coleman by letter that it elected to renew its leases for five years. In May 1987, Old Colony also notified Coleman by letter that it was exercising its renewal option. Coleman did not object to the renewals, and continued to accept the companies' rent payments.

New England and Old Colony defaulted under some of the lease provisions. The parties dispute the exact nature and timing of the defaults. It is agreed that New England failed to maintain the Kittery property. Coleman also states that Old Colony failed to pay the property taxes on the Durham and Portsmouth properties.

Circle K and its affiliates filed for Chapter 11 bankruptcy protection in May 1990. The Debtors requested, and were granted, extensions of time within which to assume or reject the Coleman leases. *See* 11 U.S.C. § 365(d)(4).

In October 1991, Coleman filed an adversary action in the bankruptcy court, seeking a declaration that the Debtors were merely tenants at will. Coleman argued that the Debtors were not assignees of the leases because the assignments had never been properly executed and violated the statute of frauds. Coleman also argued that, even if the Debtors were assignees, they had failed properly to exercise options to renew the leases, so that the leases expired either in 1987 or during the bankruptcy proceedings in 1992. Coleman also sought relief from the automatic stay so that it could take possession of the properties.

In March 1992, New England and Old Colony informed Coleman by letter of their election to extend the leases for another five year term. The Debtors then moved for summary judgment in the adversary action, asserting that: (1) they were the assignees of the leases and thus entitled to renew them; and (2) the renewals were effective even if the pre-petition

defaults had not been cured. The bankruptcy court granted the motion.

Coleman appealed to the BAP. The BAP affirmed, concluding that: (1) Coleman failed to raise a material issue of fact regarding the Debtors' status as assignees of the leases; (2) Coleman lacked standing to challenge the assignments under the statute of frauds; and (3) the Debtors successfully renewed the leases for both five-year terms even though they were in default at the time of the second extension. *Coleman Oil Co. v. Circle K Corp., (In re Circle K)*, 190 B.R. 370 (1996).

Judge Russell dissented. He agreed with the majority that the Debtors were the assignees of the leases and that Coleman lacked standing to challenge the assignments under the statute of frauds. He disagreed, however, with the majority's conclusions regarding the Debtors' post-petition extensions of the leases. He concluded that the Debtors' attempts to renew the leases for the second time were ineffective under the terms of the leases, because the Debtors were in default. *Id.* at 378-82.

II. ANALYSIS

A. Assignment Of The Leases

The first question is whether Coleman raised a triable issue of fact as to whether the Debtors were assignees of the six leases.[2] *See Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). The Debtors have relied on a series of corporate mergers and acquisitions to establish their status as assignees. Although the chain of events is somewhat intricate, we conclude that the Debtors adequately established that the leases had been assigned to them.

[2]We review de novo the BAP's decisions. *Alsberg v. Robertson (In re Alsberg)*, 68 F.3d 312, 314 (9th Cir. 1995). We independently review bankruptcy court rulings on appeal from the BAP. *Finalco, Inc. v. Roosevelt, (In re Roosevelt)*, 87 F.3d 311, 314 (9th Cir. 1996).

NPI, the parent corporation of New England and Old Colony, became an assignee of the leases by acquiring Pickering, the original lessee, in December 1983. A Plan of Liquidation evidences that transaction, and states that "Pickering will transfer all its assets" to NPI. ER 5 Exh. P. at 1. Charter then merged with NPI in 1989, after Circle K had acquired Charter in 1988. A Stock Purchase Agreement evidences Circle K's acquisition of Charter. ER 5 Exh. N.

Circle K thus became the parent corporation of New England and Old Colony. There is a written assignment of the Portsmouth and Durham leases from NPI to Old Colony dated May 1985. ER 5 Exh. B. As to the four New England leases, the Debtors produced an affidavit and a May 1989 letter from New England's counsel to Coleman. ER 7 at 2-3, Exh. 1. The affidavit is of Paul Welch, the president of New England, and he states that New England became the assignee of the four leases in March 1987. ER 7 at 2-3. The May 1989 letter confirms that information. ER 7 Exh. 1. We thus conclude that Coleman's attacks on the "paper trail" lack merit.

[1] Coleman argues that it nonetheless has raised an issue of fact because the Debtors' actions have been inconsistent with the supposed assignments. Coleman points to New England's and Old Colony's contemporaneous requests to extend some of the same leases. Coleman also points to an October 1992 retroactive written assignment of four leases to New England. As the Debtors respond, however, any inconsistent or mistaken behavior on their part does not make the actual assignments ineffective. Moreover, we conclude that such minimal evidence of equivocal behavior would be insufficient, in the face of the Debtors' other uncontradicted evidence, for a reasonable jury to find that the assignments had not occurred. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 252 (1986). We thus conclude that Coleman has failed to raise a genuine issue of material fact regarding the assignments. *See id.* ("The mere existence of a scintilla of evidence

in support of the plaintiff's position will be insufficient" to defeat summary judgment).

[2] Coleman finally contends that the assignments are invalid because the Debtors have not produced formal written instruments of transfer. There is, however, a written assignment of the Portsmouth and Durham leases from NPI to Old Colony dated May 1985. ER 5 Exh. B. In any event, the leases do not require that assignments be in writing. The leases give the lessee the right simply to assign, with the condition only that the original lessee remain primarily liable. *See* ER 7 Exh. B. Coleman's invocation of the statute of frauds is meritless. Coleman is not, merely because it is the lessor, a party to any assignments of the leases. *See* 37 C.J.S. *Statute of Frauds* § 220 (1943). The parties to the assignments do not challenge their validity; it would be for them, not Coleman, to raise the statute of frauds as a defense to enforcement of the assignments if they so chose. *See id.*; *see also* Restatement (Second) of Contracts § 144 (1982). We conclude, therefore, that the Debtors were properly granted summary judgment on this point.

B. Extension of the Leases

The next question is whether the Debtors successfully extended the leases in 1987 and 1992. The leases placed two conditions on renewal: (1) the Debtors had to give Coleman six months advance written notice of their intent to renew; and (2) the Debtors could not be in default on any lease at the time of renewal. ER 5 Exh. A at 2. Coleman contends that the Debtors failed to meet these conditions for the renewals in 1987 and in 1992.

1. Extension Of The Leases In 1987

With regard to the 1987 renewals, Coleman contends that the Debtors failed to meet both the notice and the default requirements. Coleman argues that the Debtors did not meet

the notice requirement because Old Colony and New England gave notice of extensions of leases that they had not yet been assigned. Coleman also asserts that at least the Kittery lease was in default in 1987.

[3] We conclude that the extensions in 1987 are no longer open to challenge. Whether there were any defaults and whether there was any imperfection in the way that the notice was given, all parties acted as if the extensions were effective and any objections to them have long since been waived. *See, e.g., Oxford Properties & Fin. Ltd. v. Engle*, 943 F.2d 1150, 1153-54 (9th Cir. 1991). Coleman continually accepted rent from the Debtors and otherwise treated the Debtors as lessees for many years after 1987. Coleman is estopped from asserting now, ten years later, that the leases expired in 1987. *See id.* The leases thus remained effective for the five-year term from 1987 to 1992.

2. Extension Of The Leases In 1992

[4] With respect to the 1992 post-bankruptcy-petition extension of the leases, Coleman argues that the Debtors' renewals were ineffective because the leases were in default. We agree that there were defaults under at least some of the leases.[3] There was a pre-petition default on the Kittery lease because the Debtors left the property in disrepair. There also may have been some monetary pre-petition defaults on the Durham, Portsmouth, and Epping leases. The exact nature and extent of the defaults is immaterial because, for reasons we will now explain, we conclude that the bankruptcy court had the power to permit the Debtors to extend the leases without first curing the defaults. The Debtors thus preserved their ability later to assume the leases. *See* 11 U.S.C. § 365(a).

[3]Because we conclude that the 1992 renewals were effective even though there were defaults, we need not resolve the issue of the enforceability in bankruptcy of the leases' cross-default provisions, under which a default in any lease prevents renewal of all of them.

[5] The bankruptcy court and the BAP based their rulings on the rationale underlying section 365.[4] As the BAP stated, "[t]he purpose behind § 365 is to balance the state law contract right of the creditor to receive the benefit of his bargain with the federal law equitable right of the debtor to have an opportunity to reorganize." *Coleman Oil Co.*, 190 B.R. at 376; *see also City of San Francisco Market Corp. v. Walsh, (In re Moreggia & Sons, Inc.)*, 852 F.2d 1179, 1185 (9th Cir. 1988). Section 365, in conjunction with the automatic stay provision of section 362, accordingly suspends, once the bankruptcy petition is filed, the termination of a lease that is in default; it extends[5] a debtor lessee's opportunity to cure any defaults until the debtor has the chance to decide whether to assume the lease. *See* 11 U.S.C. §§ 362, 365 (1994); *Post v. Sigel & Co., (In re Sigel & Co.)*, 923 F.2d 142, 144-45 (9th Cir. 1991). The lessor will then get the benefit of its bargain upon assumption, when the debtor lessee must cure the defaults. *See* 11 U.S.C. § 365(b)(1).

If the bankruptcy court could not allow a debtor lessee to renew a lease without first curing defaults, section 365's basic purpose would be frustrated. The debtor would be denied the benefit of section 365's "suspension of time" in order to determine whether to assume or reject the lease. *See id.* § 365(d)(4). For example, if the bankruptcy court could not permit the Debtors to exercise their renewal option without

[4]The curing of defaults in an executory contract or unexpired lease is governed by section 365, not by the more restrictive extension-of-time provisions of section 108(b). *See Moody v. Amoco Oil Co.*, 734 F.2d 1200, 1215-16 (7th Cir. 1984). We agree with the majority of the BAP that section 365 also encompasses the curing of defaults prior to the exercise of an option to renew. *See Coleman Oil Co.*, 190 B.R. at 377-78. On this appeal, neither party has contended that section 108(b) governs.

[5]The "extension" minimally is 60 days from the date of the order for relief. *See* 11 U.S.C. § 365(d)(4). But the bankruptcy court, as in this case, often grants the debtor's request to extend that period. *See id.*; *see, e.g., Willamette Waterfront, Ltd. v. Victoria Station, Inc., (In re Victoria Station Inc.)*, 875 F.2d 1380, 1384-85 (9th Cir. 1989).

curing their pre-petition defaults, the Debtors' later choice to assume or reject the leases, guaranteed by section 365, becomes flawed. If the Debtors failed to cure the defaults at renewal (as they did in this case), the leases would expire and the Debtors would be wholly unable later to exercise the choice to assume or reject the unexpired leases. On the other hand, if the Debtors cured the defaults in order to preserve their option to assume or reject, and if they later chose to reject, they would have been forced into granting a preference. In the usual case where an unexpired lease is rejected by the choice of the debtor, any pre-petition defaults become unsecured claims against the bankruptcy estate. *See e.g., Pacific Express, Inc. v. Teknetron Infoswitch Corp. (In re Pacific Express, Inc.)*, 780 F.2d 1482, 1486 (9th Cir. 1986). If, however, the Debtors have been forced to cure the pre-petition defaults in order to preserve their choice to assume or reject, then a later election to reject leaves the lessor with a preference over other pre-petition general creditors.

[6] The practical effect of requiring the Debtors to cure pre-petition defaults in order to extend the leases thus would be to require an early decision whether to assume or reject the leases. But the bankruptcy court here had explicitly extended beyond June 1992 the Debtors' time to decide whether to assume or reject. The bankruptcy court was not compelled to require a course of action that would render its extension of time illusory, thus depriving the Debtors of the opportunity to reorganize without prematurely burdening the estate with unexpired lease obligations.[6] *See Willamette Waterfront, Ltd.*, 875 F.2d at 1384-85.

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[6]Of course, the Debtors were required to perform obligations of the leases arising after the order for relief and before assumption of the leases. *See* 11 U.S.C. § 365(d)(3). The only post-petition default established here was less than $200 with regard to one property. The amount was tendered when notice of the default was given to the Debtors. The bankruptcy court characterized this default as *de minimis* and we agree. In these circumstances, the BAP did not err in concluding that, in order to preserve the choice under section 365 to assume or reject the leases, cure of this default, too, was not required for exercise of the option to renew.

We find persuasive the reasoning in *In re Webster, Clothes, Inc.*, 36 B.R. 260 (D. Md. 1984). There, the bankruptcy court implied a power under section 365 to allow a debtor lessee to exercise options. As in the present case, Webster's leases provided for options to extend, but only so long as Webster was not in default. *See id.* at 262. Webster was in default under the leases, but the court held that Webster nonetheless could extend them. *Id.* at 262-63. The court concluded that the general purpose behind section 365 supported such a result, noting that the section's goal is "the preservation of the status quo until the debtor-in-possession decides whether to assume or reject." *Id.* at 263. We recognize that *Webster* was decided before the 1984 amendments to section 365, at a time when the debtor had no obligation to exercise the choice to assume or reject a lease until confirmation of the plan. The result in *Webster* accordingly was based in part on the failure of the lessor to move to shorten the time for election. *See id.* at 264; *see also Cook United, Inc. v. Washington Distrib., Inc.*, 53 B.R. 342, 345 (N.D. Ohio 1985). But the remaining rationale of *Webster* is applicable here: a future election under section 365 to assume or reject will be rendered largely illusory if pre-petition defaults must be cured in order to keep the lease alive for the election.

[7] Coleman argues that the bankruptcy court lacks the power to "re-write" the parties' contract. *See, e.g., Shokbeton Indus., Inc. v. Shokbeton Products Corp.*, (*In re Shokbeton Indus.*), 466 F.2d 171 (5th Cir. 1972). But all kinds of interferences with contractual rights occur in bankruptcy proceedings. Section 365(a) permits a debtor to reject an executory contract or unexpired lease altogether, which wholly contravenes the contract or lease as written. The automatic stay in bankruptcy frequently prevents the enforcement of contracts according to their terms. We have held that a bankruptcy debtor may cure a default and avoid the termination of a contract even if the contract does not allow for cure. *Post*, 923 F.2d at 144-45. Thus no principle of bankruptcy or contract law precludes us from permitting the Debtors here to extend

their leases in a manner contrary to the leases' terms, when to do so will effectuate the purposes of section 365.

[8] We therefore affirm the BAP's decision that the Debtors could exercise their final option to renew the leases without first curing the pre-petition defaults. Thus renewed, the leases did not expire in 1992, and the Debtors could later assume them, curing the defaults or giving assurance of prompt cure at that time. *See* 11 U.S.C. § 365(b)(1)(A).

III. CONCLUSION

The Debtors provided ample evidence to show that they are assignees of the leases, and Coleman has not raised a material issue of fact on that issue. Coleman is estopped from asserting that Circle K's five-year extension of the leases in 1987 was ineffective; Coleman and the Debtors for years acted as if the extension had been properly executed. Finally, to effectuate the objectives of 11 U.S.C. § 365, Circle K could exercise the 1992 post-bankruptcy-petition renewal options even though there were defaults under the leases.

The judgment of the BAP is **AFFIRMED.**

RYMER, Circuit Judge, concurring in part and dissenting in part:

The path to deciding whether 11 U.S.C. § 365 allows a lessee debtor in bankruptcy to exercise an option to renew despite being in default, contrary to an express condition precedent in the lease, is uncharted. While the majority's view is plausible, I see nothing in § 365 that allows debtors to disregard their leases and renew while in default.

Because exercising the option to renew was conditioned on not being in default on the leases, and the leases were in

default at the time the debtors tried to exercise the option, the right to renew was lost. Section 365 does not extend the time to exercise the option or to meet conditions precedent. Nor does § 365 give the debtor the right to opt to renew a contract that is in default when the contract by its terms requires that a default first be cured.

To hold otherwise rewrites the lease and, as I read it, § 365. Therefore, for the reasons given by Bankruptcy Judge Russell in his BAP dissent, *Coleman Oil Co., Inc. v. The Circle K Corp. (In re The Circle K Corp.)*, 190 B.R. 370, 378-82 (1995) (Russell, B.J., dissenting), I would reverse.

Although I agree that Coleman's arguments about the chain of title and the statute of frauds fail, there are disputes of fact about who was in default and where. I would leave these issues, as well as state law forfeiture issues, to the bankruptcy court on remand.

Chapter 365

Executory Contracts and Unexpired Leases

BANKRUPTCY CODE, Section 365

(11 U.S.C. § 365)

§ 365. **Executory contracts and unexpired leases.**

(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

(b) (1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee—

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to—

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title;

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement; or

(D) the satisfaction of any penalty rate or provision relating to a default arising from any failure by the debtor to perform nonmonetary obligations under the executory contract or unexpired lease.

(3) For the purposes of paragraph (1) of this subsection and paragraph (2)(B) of subsection (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance—

(A) of the source of rent and other consideration due under such lease, and in the case of an assignment, that the financial condition and operating performance of the proposed assignee and its guarantors, if any, shall be similar to the financial condition and operating performance of the debtor and its guarantors, if any, as of the time the debtor became the lessee under the lease;

(B) that any percentage rent due under such lease will not decline substantially;

(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in

any other lease, financing agreement, or master agreement relating to such shopping center; and

(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center.

(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.

(c) The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if—

(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(B) such party does not consent to such assumption or assignment;

or

(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor;

(3) such lease is of nonresidential real property and has been terminated under applicable nonbankruptcy law prior to the order for relief; or

(4) such lease is of nonresidential real property under which the debtor is lessee of an aircraft terminal or aircraft gate at an airport at which the debtor is the lessee under one or more additional nonresidential leases of an aircraft terminal or aircraft gate and the trustee, in connection with such assumption or assignment, does not assume all such leases or does not assume and assign all of such leases to the same person, except that the trustee may assume or assign less than all of such leases with the airport operator's written consent.

(d) (1) In a case under chapter 7 of this title, if the trustee does not assume or reject an executory contract or unexpired lease of residential real property or of personal property of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected.

(2) In a case under chapter 9, 11, 12, or 13 of this title, the trustee may assume or reject an executory contract or unexpired lease of residential real property or of personal property of the debtor at any time before the confirmation of a plan but the court, on the request of any party to such contract or lease, may order the trustee to determine within a specifed period of time whether to assume or reject such contract or lease.

(3) The trustee shall timely perform all the obligations of the debtor, except those specified in section 365(b)(2), arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title. The court may extend, for cause, the time for performance of any such obligation that arises within 60 days after the date of the order for relief, but the time for performance shall not be extended beyond such 60-day period. This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f) of this section. Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title.

(4) Notwithstanding paragraphs (1) and (2), in a case under any chapter of this title, if the trustee does not assume or reject an unexpired lease of nonresidential real property under which the debtor is the lessee within 60 days after the date of the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such lease is deemed rejected, and the trustee shall immediately surrender such nonresidential real property to the lessor.

(5) Notwithstanding paragraphs (1) and (4) of this subsection, in a case under any chapter of this title, if the trustee does not assume or reject an unexpired lease of nonresidential real property under which the debtor is an affected air carrier that is the lessee of an aircraft terminal or aircraft gate before the occurrence of a termination event, then (unless the court orders the trustee to assume such unexpired leases within 5 days after the termination event), at the option of the airport operator, such lease is deemed

rejected 5 days after the occurrence of a termination event and the trustee shall immediately surrender possession of the premises to the airport operator; except that the lease shall not be deemed to be rejected unless the airport operator first waives the right to damages related to the rejection. In the event that the lease is deemed to be rejected under this paragraph, the airport operator shall provide the affected air carrier adequate opportunity after the surrender of the premises to remove the fixtures and equipment installed by the affected air carrier.

(6) For the purposes of paragraph (5) of this subsection and paragraph (f)(l) of this section, the occurrence of a termination event means, with respect to a debtor which is an affected air carrier that is the lessee of an aircraft terminal or aircraft gate—

(A) the entry under section 301 or 302 of this title of an order for relief under chapter 7 of this title;

(B) the conversion of a case under any chapter of this title to a case under chapter 7 of this title; or

(C) the granting of relief from the stay provided under section 362(a) of this title with respect to aircraft, aircraft engines, propellers, appliances, or spare parts, as defined in section 101 of section 40102 of title 49, except for property of the debtor found by the court not to be necessary to an effective reorganization.

(7) Any order entered by the court pursuant to paragraph (4) extending the period within which the trustee of an affected air carrier must assume or reject an unexpired lease of nonresidential real property shall be without prejudice to—

(A) the right of the trustee to seek further extensions within such additional time period granted by the court pursuant to paragraph (4); and

(B) the right of any lessor or any other party in interest to request, at any time, a shortening or termination of the period within which the trustee must assume or reject an unexpired lease of nonresidential real property.

(8) The burden of proof for establishing cause for an extension by an affected air carrier under paragraph (4) or the maintenance of a previously granted extension under paragraph (7)(A) and (B) shall at all times remain with the trustee.

(9) For purposes of determining cause under paragraph (7) with respect to an unexpired lease of nonresidential real property between the debtor that is an affected air carrier and an airport operator under which such debtor is the lessee of an airport terminal or an airport gate, the court shall consider, among other relevant factors, whether substantial harm will result to the airport operator or airline passengers as a result of the extension or the maintenance of a previously granted extension. In making the determination of substantial harm, the court shall consider, among other relevant factors, the level of actual use of the terminals or gates which are the subject of the lease, the public interest in actual use of such terminals or gates, the existence of competing demands for the use of such terminals or gates, the effect of the court's extension or termination of the period of time to assume or reject the lease on such debtor's ability to successfully reorganize under chapter 11 of this title, and whether the trustee of the affected air carrier is capable of continuing to comply with its obligations under section 365(d)(3) of this title.

(10) The trustee shall timely perform all of the obligations of the debtor, except those specified in section 365(b)(2), first arising from or after 60 days after the order for relief in a case under chapter 11 of this title under an unexpired lease of personal property (other than personal property leased to an individual primarily for personal, family, or household purposes), until such lease is assumed or rejected notwithstanding section 503(b)(1) of this title, unless the court, after notice and a hearing and based on the equities of the case, orders otherwise with respect to the obligations or timely performance thereof. This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f). Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title.

(e) (1) Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on—

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

(2) Paragraph (1) of this subsection does not apply to an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if—

(A) (i) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or to an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(ii) such party does not consent to such assumption or assignment;

or

(B) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor.

(f)(1) Except as provided in subsection (c) of this section, notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law, that prohibits, restricts, or conditions the assignment of such contract or lease, the trustee may assign such contract or lease under paragraph (2) of this subsection; except that the trustee may not assign an unexpired lease of nonresidential real property under which the debtor is an affected air carrier that is the lessee of an aircraft terminal or aircraft gate if there has occurred a termination event.

(2) The trustee may assign an executory contract or unexpired lease of the debtor only if—

(A) the trustee assumes such contract or lease in accordance with the provisions of this section; and

(B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease.

(3) Notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law that terminates or modifies, or permits a party other than the debtor to terminate or modify, such contract or lease or a right or obligation under such contract or lease on account of an assignment of such contract or lease, such contract, lease, right, or obligation may not be terminated or modified under such provision because of the assumption or assignment of such contract or lease by the trustee.

(g) Except as provided in subsections (h)(2) and (i)(2) of this section, the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease—

(1) if such contract or lease has not been assumed under this section or under a plan confirmed under chapter 9, 11, 12, or 13 of this title, immediately before the date of the filing of the petition; or

(2) if such contract or lease has been assumed under this section or under a plan confirmed under chapter 9, 11, 12, or 13 of this title—

(A) if before such rejection the case has not been converted under section 1112, 1208, or 1307 of this title, at the time of such rejection; or

(B) if before such rejection the case has been converted under section 1112, 1208, or 1307 of this title—

(i) immediately before the date of such conversion, if such contract or lease was assumed before such conversion; or

(ii) at the time of such rejection, if such contract or lease was assumed after such conversion.

(h) (1) (A) If the trustee rejects an unexpired lease of real property under which the debtor is the lessor and—

(i) if the rejection by the trustee amounts to such a breach as would entitle the lessee to treat such lease as terminated by virtue of its terms, applicable nonbankruptcy law, or any agreement made by the lessee, then the lessee under such lease may treat such lease as terminated by the rejection; or

(ii) if the term of such lease has commenced, the lessee may retain its rights under such lease (including rights such as those relating to the amount and timing of payment of rent and other amounts payable by the lessee and any right of use, possession, quiet enjoyment, subletting, assignment, or hypothecation) that are in or appurtenant to the real property for the balance of the term of such lease and for any renewal or extension of such rights to the extent that such rights are enforceable under applicable nonbankruptcy law.

(B) If the lessee retains its rights under subparagraph (A)(ii), the lessee may offset against the rent reserved under such lease for the balance of the term after the date of the rejection of such lease and for the term of any renewal or extension of such lease, the value of any damage caused by the nonperformance after the date of such rejection, of any obligation of the debtor

under such lease, but the lessee shall not have any other right against the estate or the debtor on account of any damage occurring after such date caused by such nonperformance.

(C) The rejection of a lease of real property in a shopping center with respect to which the lessee elects to retain its rights under subparagraph (A)(ii) does not affect the enforceability under applicable nonbankruptcy law of any provision in the lease pertaining to radius, location, use, exclusivity, or tenant mix or balance.

(D) In this paragraph, "lessee" includes any successor, assign, or mortgagee permitted under the terms of such lease.

(2) (A) If the trustee rejects a timeshare interest under a timeshare plan under which the debtor is the timeshare interest seller and—

(i) if the rejection amounts to such a breach as would entitle the timeshare interest purchaser to treat the timeshare plan as terminated under its terms, applicable nonbankruptcy law, or any agreement made by timeshare interest purchaser, the timeshare interest purchaser under the timeshare plan may treat the timeshare plan as terminated by such rejection; or

(ii) if the term of such timeshare interest has commenced, then the timeshare interest purchaser may retain its rights in such timeshare interest for the balance of such term and for any term of renewal or extension of such timeshare interest to the extent that such rights are enforceable under applicable nonbankruptcy law.

(B) If the timeshare interest purchaser retains its rights under subparagraph (A), such timeshare interest purchaser may offset against the moneys due for such timeshare interest for the balance of the term after the date of the rejection of such timeshare interest, and the term of any renewal or extension of such timeshare interest, the value of any damage caused by the nonperformance after the date of such rejection, of any obligation of the debtor under such timeshare plan, but the timeshare interest purchaser shall not have any right against the estate or the debtor on account of any damage occurring after such date caused by such nonperformance.

(i)(l) If the trustee rejects an executory contract of the debtor for the sale of real property or for the sale of a timeshare interest under a timeshare plan, under which the purchaser is in possession, such purchaser may treat such contract as terminated, or, in the alternative, may remain in possession of such real property or timeshare interest.

(2) if such purchaser remains in possession—

(A) such purchaser shall continue to make all payments due under such contract, but may, offset against such payments any damages occurring after the date of the rejection of such contract caused by the non-performance of any obligation of the debtor after such date, but such purchaser does not have any rights against the estate on account of any damages arising after such date from such rejection, other than such offset; and

(B) the trustee shall deliver title to such purchaser in accordance with the provisions of such contract, but is relieved of all other obligations to perform under such contract.

(j) A purchaser that treats an executory contract as terminated under subsection (i) of this section, or a party whose executory contract to purchase real property from the debtor is rejected and under which such party is not in possession, has a lien on the interest of the debtor in such property for the recovery of any portion of the purchase price that such purchaser or party has paid.

(k) Assignment by the trustee to an entity of a contract or lease assumed under this section relieves the trustee and the estate from any liability for any breach of such contract or lease occurring after such assignment.

(1) If an unexpired lease under which the debtor is the lessee is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the debtor's obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

(m) For purposes of this section 365 and sections 541(b)(2) and 362(b)(10), leases of real property shall include any rental agreement to use real property.

(n) (1) If the trustee rejects an executory contract under which the debtor is a licensor of a right to intellectual property, the licensee under such contract may elect—

(A) to treat such contract as terminated by such rejection if such rejection by the trustee amounts to such a breach as would entitle the licensee to treat such contract as terminated by virtue of its own terms, applicable nonbankruptcy law, or an agreement made by the licensee with another entity; or

(B) to retain its rights (including a right to enforce any exclusivity provision of such contract, but excluding any other right under applicable nonbankruptcy law to specific performance of such contract) under such contract and under any agreement supplementary to such contract, to such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law), as such rights existed immediately before the case commenced, for—

(i) the duration of such contract; and

(ii) any period for which such contract may be extended by the licensee as of right under applicable nonbankruptcy law.

(2) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, under such contract—

(A) the trustee shall allow the licensee to exercise such rights;

(B) the licensee shall make all royalty payments due under such contract for the duration of such contract and for any period described in paragraph (1)(B) of this subsection for which the licensee extends such contract; and

(C) the licensee shall be deemed to waive—

(i) any right of setoff it may have with respect to such contract under this title or applicable nonbankruptcy law; and

(ii) any claim allowable under section 503(b) of this title arising from the performance of such contract.

(3) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, then on the written request of the licensee the trustee shall—

(A) to the extent provided in such contract, or any agreement supplementary to such contract, provide to the licensee any intellectual property (including such embodiment) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment) including any right to obtain such intellectual property (or such embodiment) from another entity.

(4) Unless and until the trustee rejects such contract, on the written request of the licensee the trustee shall—

(A) to the extent provided in such contract or any agreement supplementary to such contract—

(i) perform such contract; or

(ii) provide to the licensee such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment), including any right to obtain such intellectual property (or such embodiment) from another entity.

(o) In a case under chapter 11 of this title, the trustee shall be deemed to have assumed (consistent with the debtor's other obligations under section 507), and shall immediately cure any deficit under, any commitment by the debtor to a Federal depository institutions regulatory agency (or predecessor to such agency) to maintain the capital of an insured depository institution, and any claim for a subsequent breach of the obligations thereunder shall be entitled to priority under section 507. This subsection shall not extend any commitment that would otherwise be terminated by any act of such an agency.